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TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1936

No. 260

CITY BANK FARMERS TRUST COMPANY, ASSIGNEE OF FLORENCE H. BUGBEE, PETITIONER,

vs.

IRVING TRUST COMPANY, AS TRUSTEE OF THE ESTATE OF THE UNITED CIGAR STORES COMPANY OF AMERICA, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR CERTIORARI FILED AUGUST 6, 1936.

CERTIORARI GRANTED OCTOBER 26, 1936.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1936

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UNITED STATES CIRCUIT COURT OF APPEALS

FOR THE SECOND CIRCUIT. 1

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

CITY BANK FARMERS TRUST COMPANY, assignee of Florence H. Bugbee,
Appellant,

IRVING TRUST COMPANY, as trustee of the estate of the above-named Debtor, et al.,
Appellees. 2

Statement Pursuant to Rule XIII.

This proceeding was commenced in the United States District Court for the Southern District of New York on or about October 5, 1934, by the filing of a proof of claim sworn to October 5, 1934, by the claimant, City Bank Farmers Trust Company, as assignee of Florence H. Bugbee, a former landlord of United Cigar Stores Company of America, the above-named Debtor. The Debtor filed its petition for reorganization under Section 77B of the Bankruptcy Act on or about June 9, 1934. 3

The original parties to the proceeding were said Claimant, City Bank Farmers Trust Company, Irving Trust Company, as trustee of the estate of the Debtor, and certain intervenors, to wit, Jacob Ruppert Realty Corporation, Peter Grimm, et al., as a Landlords' Protective Committee, Grayson M-P. Murphy, et al., as a Preferred Stockholders' Protective Committee, Lewis L. Strauss, et al., as a Bondholders' Protective Committee, and United Stores Corporation.

Statement Pursuant to Rule XIII.

United Stores Corporation subsequently withdrew as an intervenor, and thereafter Phoenix Securities Corporation intervened. The Debtor never appeared at nor participated in the hearing before the Special Master on the trustee's objection to the claim, nor at the hearing in the District Court upon the exceptions filed by the Claimant to the report of the Special Master recommending the disallowance of the claim, and counsel for the Debtor have notified counsel for the Claimant that it is not necessary to secure their consent to nor not to serve upon them copies of this transcript of record.

Irving Trust Company, as trustee of the estate of the Debtor, served upon the Claimant on or about April 10, 1935, a copy of its petition praying that a time be fixed by Hon. Irwin Kurtz, Special Master to whom said District Court had, by its order dated July 17, 1934, referred all claims for consideration and report, for hearing its objections to said claim, and also a notice notifying the Claimant that such hearing would be held on April 29, 1935.

The hearing before the Special Master on the trustee's objections was held before Hon. Irwin Kurtz, Special Master as aforesaid, on June 3, 1935, to which date said hearing had been duly adjourned.

The report of said Special Master dated September 18, 1935, recommended that the claim be expunged. An order of said District Court, confirming the report of the Special Master, was entered November 6, 1935. The order of said District Court allowing the appeal of the Claimant from said order entered November 6, 1935, to this Court is dated December 5, 1935.

No parties have been arrested or bail taken or property attached or arrested, and the Debtor's estate is in the possession of Irving Trust Company, as trustee as aforesaid.

Proof of Claim.

UNITED STATES DISTRICT COURT, 7

FOR THE SOUTHERN DISTRICT OF NEW YORK.

In Proceedings for Reorganization of a Corporation.—No. 59886.

Proof of Claim 5458.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor. 8

United States of America,
Southern District of New York—ss.:

At the City of New York, County of New York, State of New York, on the date hereinafter set forth, came Nelson Stuart and made oath and says that.

I.

For an individual. 9

I am the claimant. My address is.....
.....

For a copartnership.

I am a member of a copartnership, the claimant, trading as.....
(Print name legibly)
..... at .....,
..... I have been authorized by said firm to make, execute and verify this proof of claim.

Proof of Claim.

10 For a corporation.

I am an officer of CITY BANK FARMERS TRUST COMPANY, the claimant, a corporation duly organized under the laws of the State of New York, having an office at 22 William Street, New York, N. Y. and am duly authorized to make, execute and verify this proof on behalf of said corporation.

For an agent.

I am an authorized agent of.....
....., the claimant, whose address is
11 .....; this deposition is not made by the claimant in person because .....
.....
I am duly authorized by said claimant to make, execute and verify this proof, and it is within my knowledge that the claim hereinafter mentioned was incurred as and for the consideration hereinafter stated, and that such claim, to the best of my knowledge and belief, still remains unsatisfied. My address is.....
.....

12 [In case none of the foregoing paragraphs is appropriate because the claim is held by executors, trustees, co-heirs, co-distributees, etc., or for any other reason, insert here the name and address of the person executing the proof of claim, the name or names of the owners of the claim, and the capacity in which the person executing the proof of claim is acting:]

II.

United Cigar Stores Company of America, the corporation which is the debtor in the above-entitled proceeding for reorganization (hereinafter called the Debtor), on August 29, 1932, filed its voluntary petition in bankruptcy and

was adjudicated a bankrupt in a proceeding in 13
the above-mentioned Court (Docket No. 55129), and Irving Trust Company was appointed trustee in bankruptcy of said bankrupt and acted as such trustee in bankruptcy (herein called the Trustee in Bankruptcy) until June 14, 1934, the date of approval of the petition herein.

The claimant is the present owner of a claim against the Debtor, based upon or arising out of the lease, dated March 22, 1922, between Florence H. Bugbee as Landlord, and the Debtor, as Tenant, covering the premises described therein, for a term commencing prior to August 14
29, 1932, and ending on April 1, 1946, or for injury resulting from the rejection of said lease by the Trustee in Bankruptcy on or about November 11, 1932, or for damages or indemnity under a covenant or covenants contained in said lease.

The Trustee in Bankruptcy surrendered the premises covered by said lease on November 11, 1932.

[Insert date on which possession of premises was turned over, or, if that date is not known, insert date of notice from Trustee in Bankruptcy that lease was rejected.]

The landlord reentered said premises on Novem- 15
ber 11, 1932.

Except to the extent hereinafter shown, neither the Debtor nor the Trustee in Bankruptcy has paid the rent or other obligations accruing under said lease after the 1st day of September, 1932.

[If the claimant is not the landlord named in the above-described lease, give explanation of how ownership of the claim was acquired, *i. e.*, by purchase of the premises, assignment, inheritance, or otherwise:]

The claim hereby made was assigned to City Bank Farmers Trust Company by Florence H. Bugbee by an instrument of assignment acknowledged September 27, 1934.

Proof of Claim.

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III.

See Schedule "A"

The Debtor was on and before June 14, 1934, the date of the approval of the petition herein, and still is, justly and truly indebted to the claimant for amounts payable under said lease or for injury resulting from the rejection of said lease by the Trustee in Bankruptcy or for damages or indemnity under a covenant or covenants contained in said lease, computed as follows:

(1) Total net or fixed rent for entire term which has not been paid by the Debtor	$203,750.00	
(2) Total taxes, insurance, assessments, water rents or rates and other payments required to be made by Debtor for entire term which have not been paid by the Debtor (use actual amounts so far as known and estimates for the future—see footnote 1)	115,381.09	
Total lease obligations which have not been paid by the Debtor		$319,131.09
Less:		
(3) Fair rental value of leased premises from date of rejection of lease to end of term (see footnote 2)	$232,115.16	
Dividends paid in bankruptcy proceeding on any claim based on original lease	$	
Amount paid by Trustee in Bankruptcy for use and occupation of premises by such trustee	$	

(4)	Amounts paid by subtenants of Debtor to landlord under original lease for occupancy up to date of rejection of lease	891.56	233,006.72
	Total amount claimed for entire term of original lease		$ 86,124.37

Claim is hereby made against the Debtor in the amount above set forth, together with such interest thereon as may be allowed by law.

1. Explain how future taxes, etc., are estimated:

2. If all or any part of the leased premises was relet to another tenant for all or any part of the balance of the term of the original lease, the terms of the new lease should be taken into consideration in making this estimate; a copy of the new lease should be attached to this proof of claim, marked Exhibit A, and the following information should be supplied:

Name of new tenant:
Date of commencement of term of new lease:
Date of expiration of term of new lease:
Net or fixed rent per year under new lease: $
Taxes and other payments per year under new lease: $
Explain how future taxes, etc., are estimated:
State also any other facts on which estimate of fair rental value is based, stating such facts, if necessary, on a separate page as a schedule hereto:

IV.

See Schedule "B"

This claim in the amount above set forth, together with interest thereon as aforesaid, is allowable on a parity with debts which would be provable under Section 63 (a) of the Bankruptcy Act to the extent of the amount provided in subdivision (b) of Section 77B of the Bankruptcy Act, which said amount is computed as follows:

(1)	Net or fixed rent accrued up to date of surrender of premises or date of reentry by landlord, whichever first occurred, and not paid by the Debtor	$ 2,957.26

(2)	Taxes, assessments, insurance, water rents or rates and other payments accrued up to date of surrender of premises or date of reentry by landlord, whichever first occurred, and not paid by the Debtor	1,724.08	
	Total lease obligations accrued up to date of surrender of premises or date of reentry by landlord, whichever first occurred, and not paid by the Debtor		$ 4,681.34
	Less:		
	Dividends paid in the bankruptcy proceeding on any claim based on original lease	$	
	Amount paid by Trustee in Bankruptcy for use and occupation of premises by said trustee	$	
(3)	Amounts paid by subtenants of Debtor to landlord under original lease for occupancy up to date of surrender of premises or date of reentry by landlord, whichever first occurred	$ 891.56	891.56
	Unpaid lease obligations accrued up to date of surrender or reentry; whichever first occurred		$ 3,789.78
(4)	Net or fixed rent reserved in lease (without acceleration) for three years next succeeding date of surrender of premises or date of reentry by landlord, whichever first occurred, or for entire balance of term if less than three years	$ 45,000.00	

(5) Taxes, assessments, insurance, water rents or rates and other payments to be made by Debtor during three years next succeeding date of surrender of premises or date of reentry by landlord, whichever first occurred, or for entire balance of term if less than three years	24,728.07	
Total lease obligations for three year period above described, or for entire balance of term if less than three years		69,728.07
Total amount of claim allowable under Section 77B on a parity with debts which would be provable under Section 63 (a)		$ 73,517.85

Claim is hereby made against the Debtor in the amount above set forth, together with such interest thereon as may be allowed by law, on a parity with debts which would be provable under said Section 63 (a).

V.

To the extent that the total amount of the claim for the entire term of the original lease, as hereinabove set forth in subdivision III hereof, is not allowable on a parity with debts which would be provable under said Section 63 (a), said claim should be allowed in subordination to debts so provable, but in priority to the claims or interests of holders of preferred and common stock of the Debtor.

VI.

No part of the claim herein asserted has been paid, and there are no setoffs or counterclaims thereto except as follows:

The claimant has not nor has any person for

or on behalf of the claimant, to deponent's knowledge or belief, had or received, for the use or benefit of the claimant, any security for said debt, except as follows:

No judgment has been rendered therefor, nor for any part thereof, but a claim based on said lease was filed in said bankruptcy proceeding and was allowed in the amount of $. See Schedule C.

In executing and filing this proof of claim, the claimant in no way waives any rights which the claimant may have to reclaim specific assets and expressly reserves such rights.

Name ..... (L. S.)
(Individual)

By .....
Agent (if executed by Agent)

CITY BANK FARMERS TRUST COMPANY,
Affix Corporate Seal
By NELSON STUART
(Corporate Seal)

Address to which all notices should be mailed:
Mrs. Florence H. Bugbee,
c/o Richard S. Wilson, Esq.,
1018-19 Trenton Trust Bldg.,
Trenton, New Jersey.

(Seal)
Subscribed and sworn to before me
this 5th day of October, 1934.

H. WILLIAMS,
Notary Public.
Kings County Clerk's No. 531.
Kings County Register's No. 5296.
New York County Clerk's No. 823.
New York County Register's No. 5-W-538.
Commission expires March 30th, 1935.

[Schedules annexed to proof of claim having a bearing upon the amount of the claim omitted.]

Notice of Hearing on Trustee's Objection to Claim.

5458 31

DISTRICT COURT OF THE UNITED STATES,

SOUTHERN DISTRICT OF NEW YORK.

In proceedings for reorganization of a corporation. No. 59,886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

32

PLEASE TAKE NOTICE that upon the annexed petition of Irving Trust Company, Trustee of the estate the above-named Debtor, verified April 9, 1935, a hearing will be held before Hon. Irwin Kurtz, Special Master, at 15 Park Row, Borough of Manhattan, City of New York, N. Y., on April 29, 1935, at 11:30 o'clock in the forenoon, or as soon thereafter as counsel may be heard, and that at said hearing the undersigned will move this Court to have the claim referred to in said petition expunged and barred from participation in any plan of reorganization confirmed by the Court in these proceedings. 33

Dated, New York, N. Y., April 10, 1935.

Yours, etc.,

CRAVATH, DE GERSDORFF,
SWAINE & WOOD,
Attorneys and Solicitors for Irving
Trust Company, Trustee of the
Estate of United Cigar Stores
Company of America, Debtor,
Office and Post Office Address,
No. 15 Broad Street,
Borough of Manhattan,
New York, N. Y.

Notice of Hearing on Trustee's Objection to Claim.

To:

MRS. FLORENCE H. BUGBEE,
c/o Richard S. Wilson,
1018-19 Trenton Trust Bldg.,
Trenton, N. J.

ROSENBERG, GOLDMARK & COLIN,
165 Broadway,
New York, N. Y.,
Attorneys for Debtor.

M. CARL LEVINE,
535 Fifth Avenue,
New York, N. Y.,
Attorney for Jacob Ruppert
Realty Corporation.

MITCHELL, TAYLOR, CAPRON & MARSH,
20 Exchange Place,
New York, N. Y.,

and

RALPH MONTGOMERY ARKUSH,
15 Broad Street,
New York, N. Y.,
Attorneys for Landlords' Protective Committee.

SHEARMAN & STERLING,
55 Wall Street,
New York, N. Y.,

and

BERLE & BERLE,
70 Pine Street,
New York, N. Y.,
Attorneys for Preferred Stockholders' Protective Committee.

Petition of Trustee for Hearing Its Objections to Claim.

37

DAVIS, POLK, WARDWELL, GARDINER & REED,
15 Broad Street,
New York, N. Y.,
Attorneys for Debentureholders Protective Committee.

SULLIVAN & CROMWELL,
48 Wall Street,
New York, N. Y.,
Attorneys for United Stores Corporation.

38

Petition of Trustees for Hearing Its Objections to Claim.

DISTRICT COURT OF THE UNITED STATES.
SOUTHERN DISTRICT OF NEW YORK.

In proceedings for reorganization of a corporation. No. 59,886.

In the Matter
of

39

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

To the Honorable Irwin Kurtz Special Master:

The petition of Irving Trust Company, as Trustee of the estate of the above-named Debtor, respectfully shows to the Court as follows:

On June 14, 1934, your petitioner was appointed temporarily and qualified as Trustee of the estate of the above-named Debtor, and on

Petition of Trustee for Hearing Its Objections to Claim.

July 17, 1934, the appointment of your petitioner as Trustee was made permanent.

There has been filed with this Court a proof of claim numbered 5458 by City Bank Farmers Trust Company as assignee of Mrs. Florence H. Bugbee (hereinafter called the Claimant) setting forth an alleged claim of the Claimant against the Debtor in the sum of $86,124.37 with interest. Your petitioner objects to the allowance of said claim for the following reasons:

The Trustee objects to the allowance of this claim for the reason that the lease upon which the claim is based contains no indemnity clause or other provision privileging the landlord thereunder, the claimant's assignor, to hold the Debtor for rent or for damages accruing after the termination of the lease by such landlord. The Trustee is advised that said landlord re-entered the leased premises in November, 1932 and relet the same to other tenants and thereby worked a forfeiture of the lease, terminating all future obligations of the Debtor thereunder.

Your petitioner, accordingly, desires to have its objections to said claim heard and considered, and said claim expunged and barred from participation in any plan of reorganization confirmed by the Court in these proceedings.

This petition and all proceedings had thereon are not intended to affect in any way, or to waive any rights of your petitioner in regard to, the questions reserved by the Court for further determination as provided in its order of July 17, 1934 as amended, and, except as specifically stated in the foregoing objections, your petitioner reserves its right of objection, as provided by order of this Court dated November 13, 1934,

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with respect to all questions relating to the scrutiny of the circumstances of an assignment of future rent claims and the amount of the consideration paid for such assignment in determining the amount of damages to be allowed the assignee thereof, and the limitation of claims filed by committee members or agents to the actual consideration paid therefor.

WHEREFORE, your petitioner respectfully requests that a time be fixed by this Court for hearing your petitioner's objections to said claim of which due notice to the Claimant and to all 44 persons and parties who have intervened in these proceedings, or to their attorneys, shall be given by mail.

Dated, April 9, 1935.

IRVING TRUST COMPANY,
as Trustee of the Estate of United Cigar
Stores Company of America, Debtor,
by JOSEPH T. STEARNS,
Assistant Secretary.

CRAVATH, DE GERSDORFF, SWAINE & WOOD, 45
Attorneys and Solicitors for said Trustee,
No. 15 Broad Street,
Borough of Manhattan,
New York, N. Y.

Petition of Trustee for Hearing Its Objections to Claim.

46

United States of America,
Southern District of New York,
State of New York,
County of New York—ss.:

JOSEPH T. STEARNS, being duly sworn, deposes and says that he is an Assistant Secretary of Irving Trust Company, the petitioner herein, and that he has read the foregoing petition and knows the contents thereof, and is informed and verily believes that the same is true.

47

JOSEPH T. STEARNS.

Subscribed and sworn to before me this
9th day of April, 1935.

ANNE L. RANDBY.
ANNE L. RANDBY,
Notary Public,
Kings County.
Kings Co. Clk's No. 376, Reg. No. 7051.
N. Y. Co. Clk's No. 95, Reg. No. 7 R 64.
Ctf. filed N. Y. Co.
Commission expires March 30, 1937.

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Stenographic Minutes of Hearing Before Special Master on Objections to Claim.

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

(In Bankruptcy.)

No. 59886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

New York, June 3, 1935,
11:30 o'clock, A. M.

Before—IRWIN KURTZ, Esq., *Special Master.*

Hearing on Objection to Claim Designated as No. 5458.

Proceeded Pursuant to Notice.

APPEARANCES:

MESSRS. CRAVATH, DE GERSDORFF, SWAINE & WOOD, Attorneys for the Trustee, by R. L. Gilpatric and B. R. Shute, Esqs., of Counsel.

M. CARL LEVINE, Esq., Attorney for Jacob Ruppert Realty Corporation and others, Intervenors-Claimants, by David Morgulas, Esq., of Counsel.

MESSRS. BERLE & BERLE, Attorneys for Preferred Stockholders' Protective Committee, Intervenors, by Winthrop Kellogg, Esq., of Counsel; and

Stenographic Minutes of Hearing Before Special Master on Objection to Claim.

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MESSRS. SHEARMAN & STERLING, Associate Counsel, by Douglas Steimle, Esq., of Counsel.

MESSRS. MITCHELL, TAYLOR, CAPRON & MARSH, Attorneys for Landlords' Protective Committee and others, Intervenor and Claimants, by Ralph M. Arkush, Esq. and Henry L. Glenn, Esq., of Counsel.

MESSRS. SULLIVAN & CROMWELL, Attorneys for United Stores Realty Corporation, Intervenor-Claimants, by Alexander M. Grean, Jr., Esq., of Counsel.

53

MESSRS. DAVIS, POLK, WARDWELL, GARDINER & REED, Attorneys for Debentureholders' Committee, by Edward R. Wardwell, Esq., of Counsel.

The Master: This is claim No. 5458, filed by the City Bank Farmers Trust Company (Florence H. Bugbee). Claim filed in the sum of $86,124.37.

MESSRS. MITCHELL, TAYLOR, CAPRON & MARSH, Attorneys for the Claimant, by Henry L. Glenn, Esq., of Counsel.

Mr. Glenn: We offer a stipulation of the
54 facts signed by counsel for the claimant, counsel for the trustee and counsel for all the intervenors, reserving the question of the amount of damages in the event that the validity of the claim is established.

The Master: Mark it.

(Document referred to is received in evidence and marked, Claimant's Exhibit 8, of this date.)

The Master: July 3, 1935 for claimant's brief. July 17, 1935 for answering memoranda. July 24, 1935 for reply.

(Thereupon at 12:15 o'clock, A. M., the hearing was closed.)

Stipulation of Facts.

55

UNITED STATES DISTRICT COURT.

SOUTHERN DISTRICT OF NEW YORK.

In Proceedings for Reorganization of a Corporation.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

56

Stipulation of facts agreed upon by and between the undersigned relating to claim No. 5458 filed in the above matter by City Bank Farmers Trust Company.

On March 22, 1922 Florence H. Bugbee and the above named debtor entered into a written lease, whereby the said debtor leased from the said Florence H. Bugbee premises situate at the southwest corner of East State and South Broad Streets, Trenton, New Jersey, for the term of twenty years from April 1, 1926 at the yearly rent of $13,500 for the first five years of the term commencing April 1, 1926 and expiring March 31, 1931, and thereafter at the yearly rental of $15,000 for the balance of the term. Said debtor also covenanted to pay all water rents, taxes and insurance premiums. It is admitted that the copy of the lease which is attached hereto is the lease entered into between the parties.

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The said debtor entered into possession of the premises under the lease and paid monthly to the lessor its annual fixed rent to September 1, 1932 and paid to the City of Trenton annual assessed

58 taxes to July 1, 1932 and assess water rents to May 23, 1932. On August 29, 1932 said debtor was adjudicated bankrupt, the term of said lease not having yet expired. Thereafter the Irving Trust Company was appointed trustee in Bankruptcy of said debtor and on November 11, 1932, by order of the referee herein, notified the lessor of its rejection of the lease. Between the date of the adjudication in bankruptcy and the rejection of the lease, the premises were occupied by subtenants of the bankrupt, from whom the trustee collected rents and which were paid to the lessor
59 upon the order of said referee.

After the rejection of the lease, the lessor leased the premises. At the time of filing the claim herein, the leases existing were as follows:

Name of new tenant: United Perfumery Co., Inc.

Date of commencement of term: June 1, 1934.

Date of expiration of term: June 1, 1939.

Minimum fixed rent per year: $10,000.

Name of new tenant: Sylvia Rosen.

60 Date of commencement of term: Dec. 1, 1933.

Date of expiration of term: Dec. 1, 1935.

Minimum fixed rent per year: $960.

Name of new tenant: Bellcamp Stores, Inc.

Date of commencement of term: March 1, 1934.

Date of expiration of term: March 1, 1939.

Minimum fixed rent per year: $4,500.

Name of new tenant: Edward Brailove.

Date of commencement of term: Oct. 1, 1934.

Date of expiration of term: Oct. 1, 1936. 61
Fixed rent per year: $720.
Name of new tenant: The R. C. Maxwell Co.
Date of commencement of term: Nov. 15, 1932.
Date of expiration of term: Nov. 15, 1933.
Fixed rent per year: $480.

There was also existing the following verbal month to month tenancies, as follows:

John Lini, at the monthly rent of $25.
Abe Greenberg, at the yearly rent of $380. 62

Since the filing of the claim, the lessor has entered into a verbal month to month tenancy for part of said premises with So. End Republican Club, at the monthly rent of $30. All of said premises are occupied except half of the third floor having a rental value of $30 per month, which rental value is based upon rent being received from So. End Republican Club for the other half of said floor.

On June 7, 1934 the bankrupt instituted in said bankruptcy proceedings a proceeding for reorganization under the provision of Section 77B 63
of the Bankruptcy Act, as amended by the Act of June 7, 1934. Said Section 77B recognizing, within certain limits, a claim resulting from the rejection of leases, said Florence H. Bugbee assigned her claim to City Bank Farmers Trust Company by an instrument of assignment acknowledged September 27, 1934.

Upon the hearing as to this claim upon the above stipulation of facts and the supplementary statement of facts attached hereto, no question of

Stipulation of Facts.

64 the amount of damages will be in issue, such question being reserved for future determination.

Dated, May . 1935.

MITCHELL, TAYLOR, CAPRON & MARSH,
Attorneys for Claimant.

CRAVATH, DE GERSDORFF, SWAINE & WOOD,
Attorneys for Trustee.

The undersigned counsel for the intervenors in
65 the above entitled proceedings hereby consents to the filing with the Special Master of the above stipulation.

M. CARL LEVINE,
Attorney for Jacob Ruppert Realty Corporation.

BERLE & BERLE
and
SHEARMAN & STERLING,
Attorneys for Preferred Stockholders Protective Committee.

66

DAVIS, POLK, WARDWELL, GARDINER & REED,
Attorneys for Debentureholders Protective Committee.

SULLIVAN & CROMWELL,
Attorneys for United Stores Corporation.

Lease.

67

INDENTURE, made this 22nd day of March, 1922 between FLORENCE H. BUGBEE, residing at No. 231 West State St., City of Trenton, New Jersey, hereinafter called "Lessor", and UNITED CIGAR STORES COMPANY OF AMERICA, a New Jersey corporation, having an office at No. 44 West 18th Street, Borough of Manhattan, City and State of New York, hereinafter called "Lessee", WITNESSETH:

That the lessor doth lease and demise, unto the lessee, and the lessee doth hire and take from 68 the lessor, ALL THAT CERTAIN building and premises situate at the Southwest corner of East State Street and South Broad Street, in the City of Trenton and the State of New Jersey, bounded and described as follows: to wit:

BEGINNING at the intersection of the southerly line of East State Street and the westerly line of South Broad Street (said lines of said streets forming an angle of ninety-eight degrees and fifty-eight minutes turning said angle from south to west) and runs thence (1) westerly, along said line of State 69 Street nineteen and five-tenths feet, to a point, said point being opposite the center of a nine inch party wall dividing the building on the lot herein described from the one on the lot adjoining on the west, now owned by Adam Fischer; thence (2) southerly, on a line through the center of said wall, being the easterly line of said Fischer's lands (said line forming an angle of eighty-five degrees and twenty-seven minutes with the line of State Street turning said angle from east to

70 south) sixty-three and seventy-eight one-hundredths feet, to a point in the northerly face of a nine inch wall, said point being twenty-four and seventeen one-hundredths feet westerly along the face of said wall measured at right angles from the line of South Broad Street, at a point in said line of said Street distant sixty and forty-two one-hundredths feet southerly from the southwesterly corner of Broad and State Streets, said point being also the southeasterly corner of lands of said Fischer; thence (3) westerly, along the face of said wall, (forming an angle of ninety-
71 four degrees and forty-seven minutes with the line of the second course herein, turning said angle from north to west) being also the southerly line of land of said Fischer, twenty-one and thirty-three one-hundredths feet to a point, said point being opposite the center of the wall dividing the building on lands of said Fischer from the one on other lands, fronting on State Street, of Wm. I. Vannest on the west, and being also the southwesterly corner of lands of said Fischer; thence (4) southerly, parallel to the
72 line of South Broad Street, and along line of land and remaining to William I. Vannest (this line forming an angle of ninety degrees and twenty-two minutes with that of the preceding course herein, turning said angle from south to east), twenty-one and ninety-three one hundredths feet, to a point in the northerly line of a three feet wide alley leading westerly from Broad Street along the northerly line of lands late of Solomon S. and Barney V. Wolfson, late of Doctor James M. Davis; thence (5) easterly along said line of said alley (said line forming an angle of

ninety-eight degrees and fifty-one minutes with the line of the preceding course herein, turning said angle from north to east) said line being distant three feet northerly and parallel to the northerly line of land of said Wolfson's forty-five and five-tenths feet, to a point in the westerly line of South Broad Street; thence (6) northerly, along said line of said street, eighty-two and fifty-two one-hundredths feet, to the point and place of beginning (the line of this course forms an angle of ninety degrees and nine minutes with that of the preceding course herein, turning said angle from north to west). Together with the free and common use of said three feet wide alley on the south, as per agreement and release entered into by and between Joseph G. Brearley et al, and Isaac Gould et al, dated March 30, 1855 and recorded May 7, 1855 in Deed Book Liber 33, pages 7-11, in the Office of the Clerk of Mercer County, Subject, however, to the right of Adam Fischer, to build into the wall which is now the southerly boundary of his lot fronting on State Street, (being the third course of the above description) as per agreement above referred to, between the first and second parties thereto with the appurtenances; being the same premises now occupied by the lessee under certain lease dated December 13, 1915 made and executed by Wilbur F. Sadler, Jr. to the United Merchants Realty & Improvement Company.

TO HAVE AND TO HOLD the premises hereby demised unto the lessee, its successors and assigns for a term of twenty (20) years commencing on April 1, 1926 and expiring on March 31, 1946 at

the yearly rent of Thirteen Thousand Five Hundred Dollars ($13,500.00) for the first five years of the term commencing April 1, 1926 and expiring March 31, 1931, and thereafter at the yearly rental of Fifteen Thousand Dollars ($15,000.00) for the balance of the term, payable in equal monthly payments in advance on the first day of each and every month during the term.

And it is agreed by and between the parties hereto that if any rent shall be due and unpaid, or if default shall be made in any of the covenants herein contained, then it shall be lawful for the said lessor, without notice, to re-enter the said premises and to remove all persons therefrom, or to proceed by action at law for the recovery of the possession of the same.

The lessee does further covenant and agree to pay and discharge all water rents and water rates and taxes assessed, levied and imposed upon demised premises during the term of this lease within thirty (30) days after the same become due and payable, such water rates, rents and taxes to be apportioned between the parties for the first and last years of the term, the lessor to pay one-fourth and the lessee to pay three-fourths for the year 1926, and the lessor to pay three-fourths and the lessee to pay one-fourth for the year 1946. In the event this lease commences prior to April 1, 1926 as hereinafter provided then the taxes for the year in which this lease commences shall be apportioned between the parties hereto.

The lessee shall have the right to contest or review by legal proceedings or in such other manner as it deems suitable, which proceedings, if instituted, shall be conducted promptly at its own expense and free of expense to the lessor (but lessor covenants and agrees to join in such ap-

plications if required by laws, requirements, regu- 79
lations or authorities wherein premises are lo-
cated) any taxes, water rates or charges imposed
upon or against the parcel of land or building
or improvements thereon above described, and in
case any such taxes, water rates or charges shall,
as a result of any such proceedings or otherwise,
be reduced, cancelled, set aside or to any extent
discharged, and upon the determination of such
proceedings, the lessee shall pay the amount that
shall be finally assessed or imposed against said
premises or be adjudicated to be due and payable
on any such disputed or contested items. The
legal proceedings herein referred to shall include 80
appropriate appeals from any judgments, decrees
or orders and certiorari proceedings and appeals
from orders therein, but all such legal proceedings
shall be begun as reasonably soon as possible after
the imposition of any contested lien and shall be
prosecuted to final adjudication with all prompt-
ness and despatch.

And the said lessee covenants to pay to the said
lessor the said rent at the times and in the man-
ner as herein specified and to pay the said water
rates, water rents and taxes assessed, levied and
imposed upon the demised premises during the 81
term at the times and in the manner hereinbefore
prescribed, and that at the expiration of the said
term, or other determination of this lease, the
said lessee will quit and surrender the premises
hereby demised in as good state and condition as
reasonable use and wear thereof will permit,
damages by fire and the elements excepted.

And the said lessee hereby covenants and agrees
that all repairs necessary for the good and safe
condition of the demised premises during the term
of this lease, it will perform and make at its own
expense.

82 And the said lessee further covenants and agrees that it will, at its own expense, make such alterations and/or improvements upon the premises hereby demised as it shall desire, and lessor hereby consents to the making of any such alterations and/or improvements by lessee, said improvements to belong to and become the property of the lessor at the expiration or other determination of this lease.

The lessee shall at its own expense insure any building now or hereafter forming part of demised premises for the full insurable value thereof
83 in a good, reliable insurance company or companies authorized to do business in the State of New Jersey in the name of and for the benefit of lessor and shall keep said building so insured during the entire term of this lease, and all premiums upon said fire insurance policies shall be paid by lessee in addition to the rent. In the event that any building now or hereafter forming part of demised premises shall be partially damaged by fire or other casualty or happening during the term, then said building shall be restored to its condition immediately prior to such damage with due diligence by lessor and all in-
84 surance moneys collected upon any policies of insurance upon demised premises shall be paid over to lessor, who shall repair or replace the loss with the insurance money received but shall not be called upon to advance any additional sum, and the rent and taxes until such repairs shall have been made shall be apportioned in proportion to the part of the premises which is still usable. In case the building forming part of demised premises or any building hereafter erected upon the land forming part of demised premises shall be substantially destroyed by fire or other casualty or happening prior to April 1,

1943, then lessor shall erect with due diligence 85
a new building upon the land forming part of demised premises substantially similar to the building so destroyed, and all insurance moneys collected upon any policies of insurance upon the demised premises shall be paid over to the lessor, who shall expend the insurance money in replacing the building in so far as same will go but if that sum is not sufficient the lessee will supply additional funds, and any unearned rent and taxes paid in advance shall be refunded to lessee. The rent and taxes payable hereunder shall abate until the new building is ready for use and occupancy by lessee. In case the building forming 86
part of demised premises or any building hereafter erected upon the land forming part of demised premises shall be substantially destroyed by fire or other casualty or happening between April 1, 1943 and April 1, 1946 then this lease shall cease and come to an end as of the date of such destruction, and the insurance collected shall belong to the lessor and any unearned rent and taxes paid in advance by the lessee shall be refunded to it.

It is expressly understood and agreed that in the event the building now forming part of de- 87
mised premises and now occupied by lessee under lease dated December 13, 1915 between Wilbur F. Sadler, Jr., as landlord, and United Merchants Realty & Improvement Company, as tenant, which lease by its terms expires April 1, 1926, shall prior to April 1, 1926 become untenantable and be demolished or destroyed by governmental order or otherwise, and as a result thereof said lease hereinbefore in this paragraph referred to shall cease and terminate, then and in that event this lease between Florence H. Bugbee, as lessor, and United Cigar Stores Company of America, as

lessee, shall commence upon the completion of the demolition of said present building and shall continue up to and including March 31, 1946; and the rental payable by lessee to lessor shall be as follows: Ten Thousand Dollars ($10,000.00) per annum from the date of the commencement of said lease up to and including March 31, 1926, Thirteen Thousand Five Hundred Dollars ($13,500.00) per annum for the period commencing April 1, 1926 and expiring March 31, 1931, and Fifteen Thousand Dollars ($15,000.00) per annum for the balance of the term commencing April 1, 1931 and expiring March 31, 1946, excepting that no rental shall be due or payable by lessee to lessor for the first six (6) months of the term unless within such six months period the new building hereinafter referred to shall have been erected and completed and ready for occupancy by lessee. In the event the lease dated December 13th, 1915, between Wilbur F. Sadler, Jr. and United Merchants Realty and Improvement Company covering the demised premises and hereinbefore referred to, shall cease and terminate as in this paragraph provided, then and in that event the lessee covenants and agrees to promptly upon the commencement of the term at its own expense and cost to demolish the present building and erect and complete upon the land forming part of the demised premises a new building three stories in height (including the store or ground floor) with stores on the ground or grade floor and suitable for any lawful commercial and mercantile business and offices, lofts or salesrooms or apartments or other lawful purposes on the upper two floors; such new building to be erected in accordance with building laws of the City of Trenton and State of New Jersey, and the lessor covenants and agrees to promptly pay over to the

lessee a sum equal to the amount of any insurance 91
paid by insurance companies upon said present building in case it is damaged or destroyed by fire before the commencement of demolition; and the lessee covenants and agrees to indemnify and save harmless the lessor of and from any claims or demands, suits or actions at law for injuries or damages to persons or property resulting from the demolition of the old and the erection of such new building, and from the use of said building, street, streets or sidewalks in front thereof during the continuation of this lease. All provisions of this lease applicable to the present 92
building forming part of demised premises shall apply with full force and effect to the new building, if any, so to be erected by lessee, and to any other building erected in lieu or place thereof during the term of this lease. All provisions of this lease applicable to the time covered by the present lease (made by Wilbur F. Sadler, dated December 19, 1915 ending April 2, 1926) concerning insurance premiums, the collection and disposition of insurance, the payment of taxes and water rents, and the making of necessary repairs by the lessee, and its assumption of liability for damages to persons or property shall be un- 93
derstood to apply immediately upon the commencement of demolition of the present buildings by lessee.

And the said lessor covenants that the said lessee on paying the said yearly rent and performing the covenants aforesaid shall and may peaceable and quietly have, hold and enjoy the said demised premises for the term aforesaid.

And the said lessee further covenants that it will not assign this lease without first obtaining the written consent of the lessor, but the lessee may sublet the whole or any portion of the de-

94 mised premises for any lawful business not extra-hazardous on account of fire.

And it is expressly understood and agreed that this lease is to be binding upon the parties hereto, their heirs, executors, administrators, successors and assigns only in case the demolition of the present building is commenced before August 1, 1922.

IN WITNESS WHEREOF, the said lessor has hereunto set her hand and seal, and the said lessee has set its corporate seal attested by its Secretary, and caused these presents to be signed by its
95 Vice-President the day and year first above written.

Signed, sealed and delivered
In the presence of:

FLORENCE H. BUGBEE
UNITED CIGAR STORES COMPANY
OF AMERICA,
By WM. BAEDER
Vice-President.
(Seal)

96 (Acknowledgments.)

Supplemental Stipulation of Facts.

97

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

In Proceedings for Reorganization of a Corporation.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

98

Supplemental stipulation of facts agreed upon by and between the undersigned relating to claim No. 5458 filed in the above matter by City Bank Farmers Trust Company.

On November 15, 1932, immediately after rejection by the Trustee in Bankruptcy of the original lease with the United Cigar Stores Company, Florence H. Bugbee entered into a lease with Kaufman Hats, Inc., whereby she let store known as No. 5 South Broad Street for the term of five years from January 1, 1933 at the yearly rent or sum of $5500. to be paid in equal advance 99
monthly payments. Between November 15, 1932 and March 1, 1933, Kaufman Hats, Inc. became the Bellcamp Stores, Inc. and on March 1, 1933 said Florence H. Bugbee entered into a lease with Bellcamp Stores, Inc., whereby she let the said store for the term of one year from March 1, 1933 at the yearly rent of $4500. to be paid in equal advance monthly payments and ten per cent of the gross receipts in excess of $4500. per year, to be paid semi-annually. On March 1, 1934 this

100 lease was renewed, as shown by statement in original stipulation.

On the date of rejection by the Trustee in Bankruptcy of the original lease with the United Cigar Stores Company, the American Radio Company was in possession of store known as No. 1 South Broad Street as sub-tenant of the United Cigar Stores Company. Immediately thereafter Florence H. Bugbee let the said store to American Radio Company at the monthly rent of $250., which tenant remained in possession until on or about January 1, 1933. On December 3, 1932,
101 Florence H. Bugbee entered into a lease with United Perfumery Company, Inc., whereby she let No. 1 South Broad Street and all of the first floor space remaining for the term of five years to commence on February 1, 1933 at the annual rent of $10,000. payable in equal monthly installments in advance on the first day of each month for the first year and at the annual rent of $12,000. payable in equal monthly installments in advance on the first day of each month for the second, third, fourth and fifth years. On June 1, 1934 a new lease was entered into between the parties, as shown by statement in original stipulation.

102 On the date of rejection by the Trustee in Bankruptcy of the original lease with the United Cigar Stores Company, the second floor loft of the premises was in possession of Day Clothing Company as sub-tenant of the United Cigar Stores Company. Immediately thereafter Florence H. Bugbee let the said loft to Day Clothing Company at the monthly rent of $250. and said tenant remained in possession for two months. On March 20, 1933, Florence H. Bugbee entered into a lease with George Green, whereby she let one-half of said loft for the term of five years from April

15, 1933 at the yearly rent of $1110. to be paid 103
in equal monthly payments. The said George Green failed to carry out his contract and on December 1, 1933 Florence H. Bugbee entered into a lease with Sylvia Rosen for said space, as shown by statement in original stipulation. The remaining half of said second floor loft remained vacant until October 1, 1934, when Florence H. Bugbee entered into a lease with Edward Brailove, as shown by statement in original stipulation.

On the date of rejection by the Trustee in Bankruptcy of the original lease with the United Cigar Stores Company, the third floor loft of the prem- 104
ises was in possession of John Lini as sub-tenant of the United Cigar Stores Company. Immediately thereafter Florence H. Bugbee let the said loft to John Lini at the monthly rent of $70. He remained in possession of said space until sometime after the filing of the claim herein, during which possession rent was reduced to $25. per month. Since the filing of the claim, one half of said space has been rented to So. End Republican Club at the monthly rent of $30.

M. CARL LEVINE,
BERLE & BERLE, 105
SHEARMAN & STERLING,
DAVIS, POLK, WARDWELL,
GARDINER & REED,
SULLIVAN & CROMWELL,
MITCHELL, TAYLOR, CAPRON
& MARSH,
CRAVATH, DE GERSDORFF,
SWAINE & WOOD.

Notice of Making and Entry of Report of Special Master.

106

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

In Proceedings for Reorganization of a Corporation. No. 59,886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

107

Sir:

PLEASE TAKE NOTICE that the within is a true copy of a report made and entered herein on September 18, 1935, by Hon. Irwin Kurtz, Special Master herein.

Dated, September 19, 1935.

Yours, etc.,

CRAVATH, DE GERSDORFF,
SWAINE & WOOD,
Attorneys and Solicitors for Irving
Trust Company, Trustee of the
Estate of United Cigar Stores
Company of America, Debtor,
Office and Post Office Address,
No. 15 Broad Street,
New York, N. Y.

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To:

RICHARD S. WILSON, ESQ.,
Attorney for Mrs. Florence H. Bugbee,
1018-19 Trenton Trust Building,
Trenton, New Jersey.

Report of Special Master Recommending Disallowance of Claim.

109

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

In proceedings for reorganization of a corporation. No. 5458.

No. 59,886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA, Debtor.

110

To the Honorable Judges of the United States District Court, Southern District of New York:

I, IRWIN KURTZ, Special Master herein, do hereby respectfully report, as follows:

This is an application to expunge the claim of the City Bank Farmers Trust Company, Assignee of Mrs. Florence H. Bugbee, Landlord, for damages based upon the rejection of the lease herein, on November 14th, 1932, by the Irving Trust Company, as Trustee in Bankruptcy of United Cigar Stores Company of America, Bankrupt. The Trustee in Reorganization objects to the allowance thereof, for the reason that the lease was terminated by the Landlord, by her re-entry and reletting of the premises on November 15th, 1932, which it contends resulted in the termination of liability of the Tenant as a matter of law, and also by the very agreement

111

112

of the parties, in that the lease contained no covenant of indemnity or other provision for the continued liabllity of the Tenant after such termination. The Landlord urges her claim by virtue of Section 77-B of the Bankruptcy Act which was enacted on June 7th, 1934.

The situation presented herein, is as follows: On March 22nd, 1922 Florence H. Bugbee, as Landlord, entered into a lease with the United Cigar Stores Company of America (United), for certain premises located in Trenton, New Jersey,

113 for a term of twenty (20) years, commencing April 1st, 1926, at a graded rental commencing at Thirteen thousand five hundred ($13,500) Dollars per year, together with taxes, water rents, and insurance premiums.

On August 29th, 1932, the United filed its voluntary petition in bankruptcy, and was adjudicated on that day. At said time, the demised premises were not occupied by the Bankrupt but were entirely sublet to various tenants.

On November 14th, 1932 the Trustee notified the Landlord of its rejection pursuant to an order obtained from the Referee in Bankruptcy. There-

114 upon the Landlord, on the following day, November 15th, 1932, relet part of the demised premises and thereafter proceeded to relet other parts thereof. The lease contained no provisions for the continued liability of the tenant in the event of the termination of the lease.

Obviously, if this reentry by the Landlord and reletting of the premises terminated the lease, the liability of the United for further rent was also terminated as a matter of law, and particularly by virtue of the fact as aforesaid, that the lease contained no provisions for the continued liability of the United.

Report of Special Master Recommending Disallowance of Claim.

115

Therefore, upon such termination, the Landlord had no valid or legal claim whatsoever against the United for the further payment of rent; she not only had no provable claim in bankruptcy but, in fact, had no legal claim which would have survived the United's discharge in the said bankruptcy proceeding. Accordingly, she had no valid or legal claim against the United when the Petition of Reorganization herein under Section 77-B was approved on June 14th, 1934. Section 77-B of the Bankruptcy Act could not and did not create any valid and legal claims against a Debtor where none existed prior to the enactment of said Section. (Special Master's Report dated September 17th, 1935 in these proceedings recommending the disallowance of the claim of L. M. Norwood et al., #5026, based upon a termination of a lease, which did not contain any covenant of indemnity.)

116

However, the Landlord in her Brief now attacks the legal effect of her reentry as asserted by the Trustee. She urges that her resumption of control and the reletting of the premises on November 15th, 1932, immediately after the receipt of the formal notification of the rejection of the lease by the Trustee in Bankruptcy, did not as a matter of law in the State of New Jersey, where the demised premises are located, result in a termination of the lease, and the termination of all further liability for rent by the United. She contends that her reentry as aforesaid, was merely for the purpose of reletting the premises solely for the benefit of the United, and that she at no time resumed control thereof for her own account.

117

We must visualize the situation as it existed in November 1932, and the Landlord's actions in

118 accordance therewith. She undoubtedly realized that a Landlord had no provable claim in bankruptcy for future rent. Under the circumstances, everything else being equal, with the premises entirely sublet, it would have been unlikely for her to have not resumed control of the premises for her own benefit, and to have merely continued to consider the same, as the leased premises of the Bankrupt, so as to act in the control thereof, as the agent or as a representative of the Bankrupt only.

119 The stipulation of facts herein shows that immediately after the notification of the rejection by the Trustee on November 14th, 1932, that on the very next day, namely, on November 15th, 1932, the Landlord entered into a lease with the Kaufman Hat Company for a term of five years, commencing on January 1st, 1933, and also made a lease with F. C. Maxwell, for a term of one year, to commence immediately, of various portions of the premises. Obviously, the Landlord realized upon the adjudication of the Bankrupt on August 29th, 1932, that the Trustee would not adopt the lease, and accordingly she made prepa-
120 rations for her resumption of control and reletting of the premises immediately upon such formal notification, resulting in the prompt execution of the two leases, as aforesaid.

The Landlord makes no claim that at the time of the execution of these two leases, namely, with the Kaufman Hat Company and with R. C. Maxwell, that she asserted in writing or otherwise, that she was acting in a representative capacity and merely as agent for the Bankrupt. She makes no contention that she made any such assertion at any subsequent time in the various

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other leases which she made for other parts of the demised premises. She does not assert that at any time, either in writing or otherwise, she notified the Bankrupt or any other person, that in reletting of the premises, or in the collecting of rents, or in the operation and control of the premises, that her transactions were merely in a representative capacity only as agent on behalf of the Bankrupt. As a matter of fact, it was only after Section 77B of the Bankruptcy Act had been enacted on June 7th, 1934, followed by the approval of the petition in reorganization of the United herein on June 14th, 1934, that she made her instant claim herein, which she bases upon alleged rights granted to her by this Section.

122

As bearing on the Landlord's present contention, it might be well to note that she filed in the Bankruptcy proceeding, a claim for $1980.99 for alleged expenditures in restoring a party wall and closing up a common entrance in the demised premises, based upon the United's agreement to restore the demised premises *at the expiration of the term.* She received 50% dividends in the Bankruptcy proceeding, and the stipulation herein shows that this claim is also asserted in this Reorganization proceeding. Naturally, the entire basis of this claim for restoration is the expiration of the lease. The Trustee may well point to it, as showing that the Landlord, prior to the enactment of Section 77-B, by her re-entry and reletting of the premises as aforesaid, considered that the lease terminated and expired. It is significant also to note that the lease contained no provision giving the Landlord the right to re-enter for the purpose of reletting for the account of the Tenant.

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Report of Special Master Recommending Disallowance of Claim.

124

All in all, the conclusion is irresistible from the Landlord's entire course of conduct, after the adjudication in bankruptcy herein on August 29th, 1932, that she in fact, regarded the lease terminated, and that she reentered the premises and resumed control thereof solely for her own account. Accordingly, I find that the Landlord did not reenter or relet the premises merely as the agent for the Bankrupt, but she voluntarily terminated the lease and discharged the United from all further liability for rent thereunder.

125

In view of all the foregoing, the Landlord's claim herein, for future rent being without any legal basis on June 14th, 1934 when the United's petition in reorganization was approved, cannot be allowed in this proceeding.

I accordingly recommend that her claim, as aforesaid, should in all respects be disallowed and expunged.

Respectfully submitted,

IRWIN KURTZ,
Special Master.

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Dated, New York, September 18, 1935.

Exceptions of Claimant to Report of Special Master Recommending Disallowance of Claim. 127

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

In Proceedings for Reorganization of a Corporation.

No. 59,886.

In the Matter of

of 128

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

EXCEPTIONS OF CITY BANK FARMERS TRUST COMPANY TO REPORT OF HON. IRWIN KURTZ, SPECIAL MASTER, DATED SEPTEMBER 18, 1935, DISALLOWING AND EXPUNGING CLAIM NO. 5458.

Now comes City Bank Farmers Trust Company (hereinafter called the "Claimant"), and respect- 129
fully excepts to the Report of Hon. Irwin Kurtz, Special Master, dated September 18, 1935, recommending that the claim of City Bank Farmers Trust Company (No. 5458), as assignee of Florence H. Bugbee, should in all respects be disallowed and expunged, and to each and every part of said Report, and to the whole thereof, upon the ground that the same is erroneous in law and in fact, and, without limiting the generality of the foregoing:

Exceptions of Claimant to Report of Special Master Recommending Disallowance of Claim.

130

1. To so much of said Report as determines that the Claimant had no legal claim which would have survived the discharge of the Debtor in the prior bankruptcy proceeding.

2. To so much of said Report as determines that the Claimant had no legal claim against the Debtor after the enactment of Section 77B and the approval of the petition of the Debtor thereunder on June 14, 1934.

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3. To so much of said Report as determines that Section 77B could not and did not create any legal claim against the Debtor where none existed prior to its enactment.

4. To so much of said Report as determines that the landlord, Florence H. Bugbee, realized in November, 1932, that she had no provable claim in bankruptcy for future rent.

5. To so much of said Report as determines that the filing of a claim by Florence H. Bugbee, as landlord, in the bankruptcy proceeding for damages for breach of the covenant to restore indicates that she considered that the lease was terminated prior to the enactment of Section 77B.

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6. To so much of said Report as determines that Florence H. Bugbee, the landlord, regarded the lease as terminated after August 29, 1932, and that she re-entered the premises and resumed control thereof solely for her own account.

7. To so much of said Report as determines that Florence H. Bugbee, the landlord, did not

Exceptions of Claimant to Report of Special Master Recommending Disallowance of Claim.

133

re-enter or relet the premises as agent for the Debtor.

8. To so much of said Report as determines that Florence H. Bugbee, the landlord, voluntarily terminated the lease.

9. To said Report in whole and each and every part thereof, in so far as it fails to determine that Florence H. Bugbee, the landlord, had no intention at any time to relinquish the relation of landlord and tenant existing between her and the Debtor.

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10. To said Report in whole and each and every part thereof for the determination that no order should be made herein determining that the claim filed herein by the Claimant is a valid claim and allowing said claim, but reserving the question of the amount of damages for future determination.

Dated, September 24, 1935.

Respectfully submitted,

135

CITY BANK FARMERS TRUST COMPANY,

By MITCHELL, TAYLOR, CAPRON & MARSH,
Attorneys and Solicitors for Claimant.

Certificate of Special Master to District Court.

136

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

In proceedings for reorganization of a corporation No. 59,886.

Claim No. 5458.

In the Matter

of

137 UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

To the Honorable Judges of the United States District Court, Southern District of New York:

I, IRWIN KURTZ, Special Master herein, make the following report:

1. On September 18th, 1935 I recommended the disallowance of the claim of the City Bank
138 Farmers Trust Company, Assignee of Florence H. Bugbee, Landlord, for damages of an alleged breach of the lease upon a rejection thereof on November 14th, 1932 by the Irving Trust Company as Trustee in the prior Bankruptcy proceeding. I based my recommendation and my Report on the fact that the lease was terminated by the Landlord by her reentry and reletting of the premises on November 15th, 1932 which resulted in a termination of the liability of the Tenant as a matter of law and also by reason of the agreement of the parties, in that the lease

contained no covenant of indemnity or other pro- 139
vision for the continued liability after such termination; that therefore, the Landlord having no legal valid claim, that Section 77-B could not and did not create any legal claim against the Debtor which had not existed prior to its enactment.

2. On September 25th, 1935 the Claimant feeling aggrieved thereat, filed exceptions to the said Report.

3. The errors complained of in brief are—the 140
findings, as aforesaid, as to the termination of the lease by the Landlord, and the consequential termination of all liability of the Tenant by reason of which Claimant not having any legal valid claim heretofore, that none was created thereafter by the enactment of Section 77-B.

4. The respective contentions of the parties, as well as the legal question involved herein, are fully set forth in the said Report dated September 18th, 1935, to which this Court is respectfully referred.

5. I hand up herewith the following: 141

(a) Exceptions.

(b) Special Master's Report.

(c) Application to expunge.

(d) Stenographic minutes and exhibits.

Dated, New York, September 26, 1935.

IRWIN KURTZ,
Special Master.

Certificate of Special Master to District Court.

142 This Certificate will be placed on the Bankruptcy Motion Calendar in the District Court, on Wednesday October 2nd, 1935 at 10:30 A. M.

Notice thereof by mail given to:

CRAVATH, DEGERSDORFF, SWAINE & WOOD, Attorneys for Trustee, 15 Broad Street, New York City.

MITCHELL, TAYLOR, CARBON & MARSH, Attorneys for Claimant, 20 Exchange Place, New York City.

143

ROSENBERG, GOLDMARK & COLIN, Attorneys for Debtor, 165 Broadway, New York City.

M. CARL LEVINE, Attorney for Jacob Ruppert Realty Corporation, 535 Fifth Avenue, New York City.

RALPH MONTGOMERY ARKUSH, Attorney for Landlords Protective Committee, 15 Broad Street, New York City.

SHEARMAN & STERLING, Attorneys for Preferred
144 Stockholders Protective Committee, 55 Wall Street, New York City.

BERLE & BERLE, Attorneys for Preferred Stockholders Protective Committee, 70 Pine Street, New York City.

DAVIS, POLK, WARDWELL, GARDINER & REED, Attorneys for Debenture Holders Protective Committee, 15 Broad Street, New York City.

SULLIVAN & CROMWELL, Attorneys for United Stores Corporation and for Debtor in State Court actions, 48 Wall Street, New York City.

Opinion of Judge Hulbert Confirming Report of Special Master. 145

#370

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

#59,886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA, Debtor. 146

OPINION.

HULBERT, *D. J.*:

The United Cigar Stores of America was the lessee of premises in Trenton, New Jersey, under a lease from Claimant's assignor to expire on March 31, 1946, and had paid the rent due under said lease up to August 31, 1932.

On August 29, 1932, the lessee was adjudicated a bankrupt. 147

The premises at that time were in the possession of several sub-tenants.

On November 14, 1932, the Irving Trust Company, as Trustee in Bankruptcy, notified the landlord of its intention to reject the lease and the landlord thereafter relet various portions of the premises to or accepted attornments from the sub-tenants and subsequently relet various portions to new tenants.

There is nothing in the lease to indicate that any liability of the tenant was to survive reentry

118 and reletting by the landlord, or to authorize the landlord to relet as agent for the tenant, and no notice was given by the landlord to the bankrupt or the Trustee of any intention to relet the premises for the benefit of the bankrupt, or of any reletting which took place, nor did the landlord indicate in any way that she was reletting as agent for the bankrupt and that she intended to treat the bankrupt's liability under the lease as continuing until October 10, 1934, when a proof of claim was filed in the pending proceedings.

149 On or about June 9, 1934, the bankrupt filed a petition under Section 77B, and on June 14, 1934, this Court made an order approving said petition.

The landlord assigned her claim to City Bank Farmers Trust Company, agent for the Landlords' Protective Committee, on September 22, 1934, and claimant filed a proof of claim against the debtor herein for damages resulting from the rejection of the lease by the Trustee in Bankruptcy.

The Referee to whom the claim and the objections thereto were referred as Special Master, filed a report recommending that the claim be expunged and the matter comes on for review upon

150 petition of the claimant.

The Referee determined that the reentry of the landlord under the lease and her subsequent acts, terminated the liability on the part of the tenant under the lease. After a careful review of the record and examination of the briefs submitted, I concur in that determination.

I cannot perceive how Congress could, and there is nothing in Section 77B that expresses an intention to, revive an extinct claim.

If, at the time of the filing of a petition under Section 77B the statutory period for filing claims

Notice of Entry of Order of District Court Confirming Report of Special Master.

151

in a prior pending bankruptcy proceeding had not expired, but after the expiration of that time a claim were filed in the reorganization proceeding pursuant to notice to file claims in that proceeding, a debatable question might be presented, but the time to file in the original bankruptcy proceedings against United Cigar Stores had expired March 1, 1933, more than 16 months before the petition in these proceedings was filed and approved.

Petition denied and report of Referee confirmed.

Dated, N. Y., October 31, 1935. 152

HULBERT,
U. S. D. J.

Notice of Entry of Order of District Court Confirming Report of Special Master.

UNITED STATES DISTRICT COURT.
SOUTHERN DISTRICT OF NEW YORK.

In Proceedings for Reorganization
of a Corporation. 153

No. 59886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

Sirs:

PLEASE TAKE NOTICE that the within is a true copy of an order made and entered herein by the

Notice of Entry of Order of District Court Confirming Report of Special Master.

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Honorable Murray Hulbert, United States District Judge, on November 6, 1935, and filed in the office of the Clerk of the Court on November 8, 1935.

Dated, November 12, 1935.

CRAVATH, DE GERSDORFF,
SWAINE & WOOD,
Attorneys and Solicitors for Irving
Trust Company, Trustee of the Es-
tate of United Cigar Stores Com-
155 pany of America, Debtor,
Office & Post Office Address,
No. 15 Broad Street,
Borough of Manhattan,
New York, N. Y.

To:

MESSRS. MITCHELL, TAYLOR, CAPRON & MARSH,
Attorneys for City Bank Farmers
Trust Company, Assignee of
Mrs. Florence H. Bugbee,
20 Exchange Place,
156 New York, N. Y.

MESSRS. SHEARMAN & STERLING,
55 Wall Street,
New York, N. Y.

and

MESSRS. BERLE & BERLE,
70 Pine Street,
New York, N. Y.

Attorneys for Preferred Stockholders
Protective Committee.

Order of District Court Confirming Report of Special Master.

At a Special Term for Bankruptcy Motions of the United States District Court in and for the Southern District of New York, at the Court House thereof in the Borough of Manhattan, City and Southern District of New York, on the 6th day of November, 1935.

Present—HONORABLE MURRAY HULBERT,
United States District Judge.

In Proceedings for Reorganization of a Corporation.

No. 59886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA, a New Jersey Corporation,

Debtor.

On reading and filing the report, dated September 18, 1935, of Honorable Irwin Kurtz, Special Master, recommending that the claim filed herein by City Bank Farmers Trust Company, as assignee of Mrs. Florence H. Bugbee be disallowed, the exceptions to said report dated September 25, 1935, and filed herein on behalf of said claimant, the certificate of the Special Master, dated September 26, 1935, certifying to this Court the questions presented by such exceptions, and upon

Order of District Court Confirming Report of Special Master.

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the other documents and papers referred to in said report and certificate, and after hearing Messrs. Cravath, de Gersdorff, Swaine & Wood, attorneys and solicitors for Irving Trust Company, Trustee of the Estate of the above-named Debtor, by R. L. Gilpatric, Esq., of counsel, in support of the Special Master's report and Messrs. Mitchell, Taylor, Capron & Marsh, attorneys for said claimant, by Henry L. Glenn, Esq., of counsel, in opposition thereto, and after due consideration, it is, on motion of counsel for said Trustee,

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ORDERED that the report of Honorable Irwin Kurtz, Special Master, dated September 18, 1935, recommending that the claim of City Bank Farmers Trust Company, assignee of Mrs. Florence H. Bugbee, be expunged, be and the same is hereby approved and confirmed, that the exceptions filed to said report be and they hereby are overruled and denied and that said claim be and it hereby is disallowed and expunged.

HULBERT,
U. S. D. J.

162

Petition for Appeal and Order Allowing Appeal.

163

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

In Proceedings for Reorganization of a corporation. No. 59,886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor. 164

To the Honorable the Judges of the District Court of the United States, Southern District of New York:

The petitioner, City Bank Farmers Trust Company, as assignee of Florence H. Bugbee, a former landlord of United Cigar Stores Company of America, the Debtor in the above-entitled proceedings, feeling itself aggrieved for the reasons set forth in the assignment of errors hereto annexed and filed herewith, by the order of this 165
Court made and entered herein on or about November 6, 1935, approving and confirming the report of Hon. Irwin Kurtz, Special Master, dated September 18, 1935, recommending that the claim of City Bank Farmers Trust Company, as assignee of Florence H. Bugbee, be expunged, and disallowing and expunging said claim, hereby appeals therefrom to the United States Circuit Court of Appeals for the Second Circuit, and prays that leave be granted to it to appeal from said order of this Court to said United States

166 Circuit Court of Appeals, and that a citation issue as provided by law, directed to all the parties to the above-entitled proceedings, commanding them to appear before said United States Circuit Court of Appeals to do and receive what may appertain to justice to be done in the premises, and that a transcript of the record upon which said order of November 6, 1935, was based, and of all proceedings relating to said claim, duly authenticated, be transmitted to said United States Circuit Court of Appeals, and that a proper order relating to the security to be required of the appellant be made, and for such
167 other and further relief as to this Court may seem just and proper in the premises.

Dated, New York, N. Y., December 2, 1935.

CITY BANK FARMERS TRUST COMPANY,
By MITCHELL, TAYLOR, CAPRON & MARSH,
Its Attorneys and Solicitors.

MITCHELL, TAYLOR, CAPRON & MARSH,
Attorneys and Solicitors for
City Bank Farmers Trust
168 Company, as aforesaid,
Office and Post Office Address,
No. 20 Exchange Place,
New York, N. Y.

Petition for Appeal and Order Allowing Appeal.

United States of America,
Southern District of New York,
County of New York, 169
State of New York—ss.:

HENRY L. GLENN, being duly sworn, deposes and says: That he is associated with the firm of Mitchell, Taylor, Capron & Marsh, attorneys and solicitors for City Bank Farmers Trust Company, the petitioner named in the foregoing petition; that he has read the said petition and knows the contents thereof; that the same is true to his own knowledge, except as to the matters therein stated to be alleged on information and belief, and as to those matters, he believes it to be true. 170

HENRY L. GLENN.

Sworn to before me this
5th day of December, 1935.

JOHN T. COLLINS,
Notary Public,
Queens County.
Queens Co. Clk's No. 3108, Reg. No. 7413.
N. Y. Co. Clk's No. 903, Reg. No. 7 C 556.
Commission Expires March 30, 1937.

ORDERED, that leave to appeal as prayed for in the foregoing petition be allowed, and that 171 a certified transcript of the record on which the order appealed from is based and of all proceedings relating to the claim described in said petition be transmitted to the Circuit Court of Appeals for the Second Circuit; and it is further

ORDERED, that a bond for costs on appeal be fixed in the sum of $250.

Dated, December 5th, 1935.

HENRY W. GODDARD,
United States District Judge for the
Southern District of New York.

Assignment of Errors.

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DISTRICT COURT OF THE UNITED STATES,

SOUTHERN DISTRICT OF NEW YORK.

In Proceedings for Reorganization of a Corporation.—No. 59,886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

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Now comes City Bank Farmers Trust Company, as assignee of Florence H. Bugbee, a landlord-creditor in the above-entitled proceedings, and files the following assignment of errors upon which it will rely upon prosecution of the appeal in the above-entitled proceedings from the order of the United States District Court for the Southern District of New York made and entered on or about November 6, 1935, and says that said order dated November 6, 1935, was and is erroneous in law and in fact in that it affirms

174 and approves the report of Hon. Irwin Kurtz, Special Master, dated September 18, 1935, recommending that the claim of City Bank Farmers Trust Company, as assignee of Florence H. Bugbee, be expunged, and disallowing and expunging such claim, and, without limiting the generality of the foregoing, in that it affirms and approves:

1. So much of said report as determines that City Bank Farmers Trust Company (hereinafter sometimes called the "Claimant"), as assignee as aforesaid, had no legal claim which would have

survived the discharge of the Debtor in the bankruptcy proceeding preceding the above-entitled reorganization proceedings. 175

2. So much of said report as determines that the Claimant had no legal claim against the Debtor after the enactment of Section 77B, and the approval of the petition of the Debtor herein on June 14, 1934.

3. So much of said report as determines that Section 77B could not and did not create any legal claim against the Debtor where none existed prior to its enactment, as applied to the facts of this case. 176

4. So much of said report as determines that the landlord, Florence H. Bugbee, realized in November, 1932, that she had no provable claim in bankruptcy for future rent.

5. So much of said report as determines that the filing of a claim by Florence H. Bugbee, the landlord, in said prior bankruptcy proceeding for damages for breach of the covenant to restore indicates that she considered that the lease was terminated prior to the enactment of Section 77B. 177

6. So much of said report as determines that Florence H. Bugbee, the landlord, regarded the lease as terminated after August 29, 1932, and that she re-entered the premises and resumed control thereof solely for her own account.

7. So much of said report as determines that Florence H. Bugbee, the landlord, did not re-enter or relet the premises as agent for the Debtor.

178 8. So much of said report as determines that Florence H. Bugbee, the landlord, voluntarily terminated the lease.

The court also erred in that it did not disaffirm the whole of said report and did not determine the claim of the Claimant to be a valid claim provable and allowable under Section 77B, reserving the question of the amount of damages for future determination; and in that the court did not hold that under the law of New Jersey the Debtor was not relieved under the facts and circumstances set forth in the stipulation of facts
179 made by the parties herein from its obligations under the lease by reletting; and in that the court did not hold that, whether or not the Debtor was so relieved from its obligations under the lease under the New Jersey law by said reletting, the claim of the Claimant is provable and allowable herein under Section 77B, reserving the question of the amount of damages for future determination.

The court also erred in law and in fact in failing to determine that Florence H. Bugbee, the landlord, had no intention at any time to relin-
180 quish the relation of landlord and tenant existing between her and the Debtor.

The court also erred in holding that the provability and allowability of the claim of the Claimants herein was dependent upon the fact that the time for the filing of claims in the bankruptcy proceeding which was pending prior to the institution of the above-entitled proceeding under Section 77B had expired prior to the filing of the petition herein.

WHEREFORE, the Claimant prays that said order of November 6, 1935, be reversed and that the

Admission of Service of Copy of Citation and Bond on Appeal.

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aforesaid claim be determined to be provable and allowable herein in such amount as may be hereafter established by the Claimant at a hearing to be held before the Special Master for such purpose.

Dated, December 2, 1935.

MITCHELL, TAYLOR, CAPRON & MARSH,
Attorneys and Solicitors for
City Bank Farmers Trust
Company, as assignee of Flor-
ence H. Bugbee,
Office and Post Office Address,
No. 20 Exchange Place,
Borough of Manhattan,
New York, N. Y.

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Admission of Service of Copy of Citation and Bond on Appeal.

UNITED STATES DISTRICT COURT,
SOUTHERN DISTRICT OF NEW YORK.

183

In the Matter
of
UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

Service of a copy of the Citation and Bond on Appeal in the above entitled proceeding with

Admission of Service of Copy of Citation and Bond on Appeal.

184 notice of filing is hereby admitted this 6th day of December, 1935.

Copy received December 6, 1935.

ROSENBERG, GOLDMARK & COLIN,
Attorneys for Debtor.

CRAVATH, DEGERSDORFF, SWAINE & WOOD,
Attorneys for Irving Trust Company, Trustee for the Estate of United
185 Cigar Stores Company of America.

BERLE & BERLE
and
SHEARMAN & STERLING,
Attorneys for Stockholders' Protective Committee.

DAVIS, POLK, WARDWELL, GARDINER & REED,
Attorneys for Debentureholders' Protective Committee.

186 Copy received December 6, 1935.

SULLIVAN & CROMWELL,
Attorneys for United Stores Corporation.

M. CARL LEVINE,
Attorney for Jacob Ruppert Realty Corp.

MILBANK, TWEED, HOPE & WEBB,
Attorneys for Phoenix Securities Corp.

Citation.

By the Honorable Henry W. Goddard, one of the United States District Court Judges for the Southern District of New York, in the Second Circuit, to Irving Trust Company, as trustee of the estate of United Cigar Stores Company of America, Debtor, United Stores Company of America, United Cigar Stores Company of America, Jacob Ruppert Realty Corporation, Grayson M-P. Murphy, G. W. Baker, William de Krafft and Benjamin Graham, as a Preferred Stockholders' Protective Committee, Lewis L. Strauss, Burnett Walker and Maurice Wertheim, as a Debentureholders' Protective Committee, and Peter Grimm, Stewart C. Pratt and W. Howard Wright, as a Landlords' Protective Committee, Phoenix Securities Corporation, GREETING:

YOU ARE HEREBY CITED and admonished to be and appear before a United States Circuit Court of Appeals for the Second Circuit, to be holden at the Borough of Manhattan, in the City of New York, in the District and Circuit above named on the 4th day of January, 1936, pursuant to a petition for appeal and an order filed in the Clerk's Office of the District Court of the United States for the Southern District of New York, allowing such petition for appeal in "In the Matter of United Cigar Stores Company of America, Debtor (In proceedings for reorganization of a corporation, No. 59,886)," wherein City Bank Farmers Trust Company, as assignee of Florence H. Bugbee, is the appellant and you are appellees, to show cause, if any there be, why the order of this Court in said petition mentioned should not be corrected and why speedy justice should not be done to the parties in that behalf.

190 GIVEN UNDER MY HAND at the Borough of Manhattan, in the City of New York, in the District and Circuit above named, this 5th day of December, in the year of our Lord one thousand nine hundred and thirty-five and of the Independence of the United States the one hundred and sixtieth.

HENRY W. GODDARD,
United States Judge for the Southern District of New York in the Second Circuit.

C.W.

191

192

Bond for Costs on Appeal.

193

(Emblem)

MASSACHUSETTS BONDING AND INSURANCE COMPANY
Home Office, Boston, Massachusetts

DISTRICT COURT OF THE UNITED STATES OF AMERICA,

FOR THE SOUTHERN DISTRICT OF NEW YORK.

IN THE SECOND CIRCUIT.

In Proceedings for Reorganization of a Corporation. 194
No. 59,886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

The Petitioner, City Bank Farmers Trust Company, as assignee of Florence H. Bugbee, a 195
former landlord of United Cigar Stores Company of America, the Debtor.

KNOW ALL MEN BY THESE PRESENTS, That Massachusetts Bonding and Insurance Company, a corporation organized under the laws of the Commonwealth of Massachusetts, authorized to transact business in the State of New York, having an office and place of business at 130 William Street, Borough of Manhattan, City of New York, is held and firmly bound unto Irving Trust Company, as

196 Trustee of the Estate of United Cigar Stores Company of America, Debtor, United Stores Company of America, United Cigar Stores Company of America, Jacob Ruppert Realty Corporation, Grayson M-P. Murphy, G. W. Baker, William deKrafft and Benjamin Graham, as a Preferred Stockholders' Protectjve Committe, Lewis L. Strauss, Burnett Walker and Maurice Wertheim, as a Debentureholders' Protective Committee, and Peter Grimm, Stewart C. Pratt and W. Howard Wright, as a Landlords' Protective Committee, Phoenix Securities Corporation, in the sum of Two hun-
197 dred fifty and 00/100 ($250.00) Dollars, to be paid to the said Irving Trust Company, as Trustee of the Estate of United Cigar Stores Company of America, Debtor, United Stores Company of America, United Cigar Stores Company of America, Jacob Ruppert Realty Corporation, Grayson M-P. Murphy, G. W. Baker, William deKrafft and Benjamin Graham, as a Preferred Stockholders' Protective Committee, Lewis L. Strauss, Burnett Walker and Maurice Wertheim, as a Debentureholders' Protective Committee, and Peter Grimm, Stewart C. Pratt and W. Howard Wright, as a Landlords' Protective Committee, Phoenix
198 Securities Corporation, for the payment of which, well and truly to be made, the said Massachusetts Bonding and Insurance Company binds itself, its successors and assigns, jointly and severally, firmly by these presents.

Sealed with its seal and dated this 5th day of December, in the year of our Lord One Thousand Nine Hundred and Thirty-five.

WHEREAS, CITY BANK FARMERS TRUST COMPANY, as assignee of Florence H. Bugbee, a former

landlord of United Cigar Stores Company of America, the Debtor, has prosecuted an appeal to the United States Circuit Court of Appeals for the Second Circuit, to reverse the order dated the 6th day of November, 1935, rendered in the above entitled suit, in the District Court of the United States for the Southern District of New York. 199

NOW, THEREFORE, the condition of this obligation is such, that if the above named City Bank Farmers Trust Company, as assignee of Florence H. Bugbee, a former landlord of United Cigar Stores Company of America, the Debtor, shall prosecute said appeal to effect, and answer all damages and costs if it fail to make said appeal good, then this obligation shall be void, otherwise the same shall be and remain in full force and virtue. 200

MASSACHUSETTS BONDING AND
INSURANCE COMPANY,
By W. C. BILLINGS,
Attorney-in-Fact.

Attest GARRETT B. CARMAN,
Attorney-in-Fact. 201

(Verification, etc.)

Approved 12/6/35.

H. W. GODDARD,
U. S. D. J.

Filed 12/6/35.

Stipulation as to Record.

UNITED STATES DISTRICT COURT,

202 SOUTHERN DISTRICT OF NEW YORK.

In the Matter

of

UNITED CIGAR STORES COMPANY of AMERICA,
Debtor.

CITY BANK FARMERS TRUST COMPANY, assignee of Florence H. Bugbee,
Appellant,

IRVING TRUST COMPANY, as trustee of the estate of the above-named Debtor, et al.,
203 Appellees.

IT IS HEREBY STIPULATED AND AGREED, that the foregoing is a true transcript of the record of the United States District Court for the Southern District of New York in the above-entitled matter as agreed on by the parties, and that the Clerk of said Court may certify the same as correct.

Dated, January 13th, 1936.

MITCHELL, TAYLOR, CAPRON & MARSH,
204 Attorneys for Claimant, City Bank Farmers Trust Company.

CRAVATH, DEGERSDORFF, SWAINE & WOOD,
Attorneys for Irving Trust Company, as trustee.

BERLE & BERLE
and

SHEARMAN & STERLING,
Attorneys for Stockholders' Protective Committee.

DAVIS, POLK, WARDWELL, GARDINER & REED,
Attorneys for Debentureholders' Protective Committee. 205

M. CARL LEVINE,
Attorney for Jacob Ruppert Realty Corporation.

MILBANK, TWEED, HOPE & WEBB,
Attorneys for Phoenix Securities Corporation.

MITCHELL, TAYLOR, CAPRON & MARSH,
Attorneys for Landlords' Protective Committee. 206

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Clerk's Certificate.

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UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

In the Matter

of

UNITED CIGAR STORES COMPANY of AMERICA,
Debtor.

CITY BANK FARMERS TRUST COMPANY, assignee of Florence H. Bugbee,

209 Appellant,

IRVING TRUST COMPANY, as trustee of the estate of the above-named Debtor,

Appellee.

I, CHARLES WEISER, Clerk of the District Court of the United States of America for the Southern District of New York, do hereby CERTIFY that the foregoing is a correct transcript of the record of the said District Court in the above-entitled matter as agreed upon by the parties.

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IN TESTIMONY WHEREOF, I have caused the seal of the said Court to be hereunto affixed, at the City of New York, in the Southern District of New York, this 14th day of January, in the year of our Lord one thousand nine hundred and thirty-six, and of the Independence of the said United States the one hundred and sixty-first.

CHARLES WEISER,
Clerk.

(Seal)

[fol. 71] UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT, OCTOBER TERM, 1935

Argued March 4, 1936. Decided April 6, 1936

No. 312

In the Matter of

UNITED CIGAR STORES COMPANY OF AMERICA, Debtor

CITY BANK FARMERS TRUST COMPANY, Assignee of Florence H. Bugbee, Appellant

IRVING TRUST COMPANY, as Trustee of the Estate of the Above-Named Debtor, et al., Appellees

Appeal from the District Court of the United States for the Southern District of New York

Before Manton, Augustus N. Hand, and Chase, Circuit Judges

Appeal from an order of the District Court for the Southern District of New York in reorganization proceedings under section 77B of the Bankruptcy Act (11 U. S. C. A. § 207) disallowing and expunging a landlord's claim for damages and loss of rent because of the rejection of a lease by a trustee in the bankruptcy proceedings of the debtor pending prior to the filing of the petition herein.

Mitchell, Taylor, Capron & Marsh, of New York City (Rollin Browne and Henry L. Glenn, both of New York City, of counsel), for claimant-appellant.

Cravath, de Gersdorff, Swaine & Wood, of New York City (Wm. D. Whit-, Donald C. Swatland, R. L. Gilpatric, and B. R. Shute, all of New York City, of counsel), for the reorganization trustee.

Shearman & Sterling and Berle & Berle, all of New York City (Sanford H. E. Freund, Winthrop H. Kellogg, and Douglas B. Steimle, all of New York City, of counsel), for appellees herein Preferred Stockholders' Protective Committee.

John Gerdes and John Godfrey Saxe, both of New York City, and Edward B. Lucius, of Chicago, Ill., amici curiæ.

CHASE, Circuit Judge:

The appellant is the assignee of a claim by a landlord who owned premises in Trenton, N. J., which were leased to the debtor for a term of twenty years beginning April 1, 1926. The debtor occupied no part of the leased premises itself, but sublet them as of right it might under the lease. On August 29, 1932, the debtor filed a voluntary petition in bankruptcy and was then adjudicated a bankrupt. At that time its rent had been paid in full. Its duly qualified trustee found the lease burdensome and rejected it, pursuant to an order obtained for that purpose, on November 11, 1932, paying over to the landlord all rents it had in the meantime collected.

The landlord re-entered without notice in accordance with such a right reserved in the lease, and made structural [fol. 72] changes in the premises to restore them to the condition they were in when leased by rebuilding a party wall and closing up a common entrance, all at an expense of $1,980.99. The lease provided that, at termination, all improvements made by the lessee should belong to and become the property of the lessor, but there was no provision that, upon termination before the expiration of the term and reentry by the landlord, the premises might be relet for the lessee's account and that the lessee should be liable for any deficiency. The landlord did relet without notice to the lessee.

The issue is whether the landlord has a claim for damages because of injury occasioned by the rejection of the lease by the trustee in the prior bankruptcy proceeding.

Whether such a claim is allowable under section 77B (b) (10), 11 U. S. C. A. § 207 (b) (10), depends upon whether, under the applicable state law, it is capable of proof on the merits. See In re United Cigar Stores Co. of America (Otis), — F. (2d) — (C. C. A.); In re United Cigar Stores Co. of America (Meadows), — F. (2d) — (C. C. A.)—both decided today. Section 77B makes such a claim provable provided there is evidence in support of it which constitutes proof as a matter of law. So there is no barrier confronting the appellant on the ground of provability because the proceeding in which the attempt to prove is made is a proceeding in bankruptcy under section 77B.

But whether the order should be affirmed depends not alone upon that. It was necessary for the appellant to

prove recoverable damages as a result of the rejection. When the trustee in bankruptcy rejected the lease, such rights to rent under subleases as the lessee had originally reverted to the bankrupt subject to the lessor's equitable lien upon them to secure the payment of rent under the main lease. In re United Cigar Stores Co. of America (Reisenweber's, Inc., v. Irving Trust Co.), 69 F. (2d) 513 (C. C. A.). When, however, the landlord re-entered, as it did at once, under a re-entry clause all rights of the lessee came to an end. Ordinarily such re-entry, in the absence of a covenant for continuing liability for rent, also cuts off all liability of the lessee for future rent. In re Sherwoods, Inc. (C .C. A.) 210 F. 754, Ann. Cas. 1916A, 940. When the landlord accepts surrender of the premises, he cannot have possession and use and still collect any part of the rent reserved in a lease which no longer confers any rights in the premises upon the lessee unless the lease contains a covenant to that effect. We do not find that the law of New Jersey is different in principle from the general rule in this respect. Only in the proof of surrender to, and acceptance by, the landlord does there seem to be a distinction. Apparently proof that a lease was rejected by a receiver in bankruptcy of the lessee, that the lessor re-entered and relet without notice to the lessee of acceptance of surrender or of an intention to relet for the lessee's account, is not sufficient as a matter of law to show a surrender and acceptance of the leased premises. Liskovsky v. Blau, 114 N. J. Law, 324, 176 A. 562. See, also, Dolton v. Sickel, 66 N. J. Law, 492, 49 A. 679; Banks v. Berliner, 95 N. J. Law, 267, 113 A. 321. But here the evidence went beyond that and showed that the landlord had made substantial changes in the premises indicative of the resumption of dominion over them inconsistent with the continuing status of landlord and tenant under the lease. These acts together show such an unequivocal breaking off of the relationship which before existed under the lease that the landlord must be held to have accepted a surrender of the premises as a matter of law in consequence of what was done. Sypherd v. Myers, 80 N. J. Law, 321, 79 A. 340; Fink v. Browe Co. (N. J. Ch.) 99 A. 926. Hence the necessary proof of surrender and acceptance which ended this debtor's liability for future rent under the lease made it impossible to show on the merits that the appellant's assignor sustained any damages from injury by the rejection of the

lease. It therefore has no claim susceptible of proof as a matter of law. Section 77B did not create — rights to form the basis of claims but only enlarged the remedy to make some valid claims provable in proceedings under section 77B which were not before provable in bankruptcy. See In re United Cigar Stores Co. of America (Otis), supra, and In re United Cigar Stores Co. of America (Meadows), supra.

Order affirmed.

[fol. 73] UNITED STATES CIRCUIT COURT OF APPEALS, SECOND CIRCUIT

At a stated term of the United States Circuit Court of Appeals, in and for the Second Circuit, held at the United States Court House in the City of New York, on the 13th day of April, one thousand nine hundred and thirty-six.

Present: Hon. Martin T. Manton, Hon. Augustus N. Hand, Hon. Harrie B. Chase, Circuit Judges.

In the Matter of UNITED CIGAR STORES COMPANY OF AMERICA, DEBTOR

CITY BANK FARMERS TRUST COMPANY, as Assignee, etc., Appellant

Appeal from the District Court of the United States for the Southern District of New York

This cause came on to be heard on the transcript of record from the District Court of the United States for the Southern District of New York, and was argued by counsel.

On Consideration Whereof, it is now hereby ordered, adjudged, and decreed that the order of said District Court be and it hereby is affirmed with costs.

It is further ordered that a Mandate issue to the said District Court in accordance with this decree.

Wm. Parkin, Clerk.

[fol. 74] [Endorsed:] United States Circuit Court of Appeals, Second Circuit. In re United Cigar Stores Company of America (City Bank). Order for Mandate. United States Circuit Court of Appeals, Second Circuit. Filed April 13, 1936. William Parkin, Clerk.

[fol. 75] [Stamp:] United States Circuit Court of Appeals, Second Circuit, Filed Apr. 14, 1936. William Parkin, Clerk

14509

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

In the Matter of

UNITED CIGAR STORES COMPANY OF AMERICA, Debtor

CITY BANK FARMERS TRUST COMPANY, Assignee of Florence H. Bugbee, Appellant

IRVING TRUST COMPANY, as Trustee of the Estate of the Above-named Debtor, et al., Appellees

On Appeal from the United States District Court for the Southern District of New York

PETITION FOR REHEARING

To the United States Circuit Court of Appeals for the Second Circuit and the Judges Thereof:

Comes now City Bank Farmers Trust Company, assignee of Florence H. Bugbee, the appellant herein, and presents this its petition for a rehearing and in support thereof respectfully shows:

The decision of this Court is wrong on the facts and on the law, in that

(1) it has imported into the case an issue not presented by the record and therefore not argued by appellant;

(2) it has considered as determinative of such issue a fact which is not contained in the stipulation of facts on [fol. 76] which the case was submitted and which opposing counsel expressly conceded to be unsupported by any evidence in the record; and

(3) it has applied an erroneous rule of law to such fact.

The Special Master found that a surrender of the lease was effected by the landlord re-entering and reletting the

premises without notice to the tenant. The District Court confirmed the report, over appellant's exceptions (fols. 129, 132).

This Court held that the re-entry and reletting did not effect a surrender, but affirmed the decision on the ground that a surrender had occurred because of the acts of the landlord in making changes or alterations in the demised premises after the tenant's abandonment. This Court stated:

"The landlord re-entered without notice in accordance with such a right reserved in the lease, and made structural changes in the premises to restore them to the condition they were in when leased, by rebuilding a party wall and closing up a common entrance, all at an expense of $1980.99."

"But here the evidence went beyond that [re-entry and reletting] and showed that the landlord had made substantial changes in the premises indicative of the resumption of dominion over them inconsistent with the continuing status of landlord and tenant under the lease."

The alleged fact upon which this Court's decision was thus based is entirely unsupported by the evidence. Counsel for the Trustee stated on the argument that the land-[fol. 77] lord had made substantial alterations in the premises, but, upon our objecting to his statement, he subsequently conceded expressly that the alleged fact did not appear in the record.

The case was submitted to the Special Master on two written stipulations of fact, which constituted the only evidence in the case (fol. 54). These stipulations (fols. 55 and 97) contain no reference whatever to any alterations, changes, improvements, repairs or restorations to the premises having been made at any time by the landlord or by the tenant.

The Trustee's sole objection to the claim (fol. 41), was as follows:

"The Trustee is advised that said landlord re-entered the leased premises in November, 1932, and relet the same to other tenants and *thereby* worked a forfeiture of the lease, terminating all future obligations of the Debtor thereunder." (Italics supplied.)

The claim was thus submitted to the Special Master on the issue raised by such objection and on the evidence contained in the stipulations, which obviously were drawn with an eye to the only issue presented.

To support his conclusion that the landlord, by re-entering and reletting, had intended to accept a surrender rather than to relet for the account of the tenant, the Special Master, sua sponte, made the following statement (fol. 122):

"As bearing on the Landlord's present contention [that her reentry and reletting did not effect a surrender] it might be well to note that she filed in the Bankruptcy proceeding, a claim for $1980.00 for alleged expenditures in **restoring** a party wall and closing up a common entrance [fol. 78] in the demised premises, based upon the United's agreement to **restore** the demised premises *at the expiration of the term.* She received 50% dividends in the bankruptcy proceeding and the stipulation herein shows that this claim is also asserted in this Reorganization proceeding. Naturally, the entire basis of this claim for restoration is the expiration of the lease. The trustee may well point to it, [although the Trustee, for reasons best known to itself, had not pointed to it] as showing that the landlord, prior to the enactment of Section 7B **by her re-entry and reletting** of the premises, as aforesaid, considered that the lease terminated and expired." (Blackface and matter in brackets, but not italics, supplied.)

This Court must have assumed, from the above-quoted remarks of the Special Master, that there was evidence showing the restoration of the premises. Not only was such assumption wrong, but there was not anything in the stipulations to show that a claim had been filed in the bankruptcy proceeding for the cost of any such restoration, thus showing that these matters were not considered within the issue.

(A) The Court has misapprehended the effect under the New Jersey law of the landlord's restoration of premises to their original condition.

Although the facts are not in the record, the inferences which legitimately may be drawn from this Court's finding are as follows:

The tenant of the demised building, who also occupied the adjoining building, tore out the dividing wall in order to make one large combined space and cut a common en- [fol. 79] trance on the line of the old wall. The tenant defaulted and abandoned, whereupon the landlord had the right to resume possession and relet for the tenant's account. When the landlord re-entered for that purpose, she found a partially demolished building, and she rebuilt the wall and closed up the common entrance in order to restore the building and make it possible for her to relet.

The Court cited two cases in support of its conclusion—Sypherd v. Myers, 79 Atl. 340 and Fink v. Browe, 99 Atl. 926. In the Sypherd case it did not appear that any repairs or alterations whatever had been made; the Fink case merely held that "making changes and alterations therein that were not necessary as repairs for the preservation of the building", among other acts on the part of the landlord, indicated an intention on the landlord's part to accept a surrender. But it has never been held in New Jersey, nor elsewhere, so far as we know, that the making by the landlord of repairs or alterations merely necessary to restore the premises to the condition in which they existed at the commencement of the term is indicative of an acceptance of a surrender.

In Meeker v. Spalsbury, 66 N. J. L. 60, where a surrender was found, the landlord remodelled the building, which had been leased as a hotel, so that it could be used as either a hotel or for flats. When the work was begun the premises were already in good condition and repair.

That mere restoration of premises to their original condition does not effect a surrender is settled by the case of Zabriskie v. Sullivan, 80 N. J. L. 673, aff'd 82 N. J. L. 545, in which the alterations made by the landlord were apparently those necessary to restore the premises to their original condition, the lease containing a covenant by the [fol. 80] tenant to surrender the premises in good condition at the expiration of the term, but no covenant to repair.* The Supreme Court said (at p. 676):

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*The lease in the instant case contains both covenants (fol. 81).

"The reparation of the premises by the landlord was also for the benefit of the tenant, for it relieved him of his duty to repair and increased the likelihood of securing a tenant."

See also Liskovsky v. Blau, 114 N. J. L. 324, and Banks v. Berliner, 95 N. J. L. 267, applying the same rule to necessary repairs.**

The rule is clearly stated by Schnebly, Operative Facts in Surrenders, 22 Ill. L. Rev. 117, 129.

"Another question which arises is whether or not a surrender results from the fact that the lessor has made repairs before reletting. The making of necessary repairs ought not to be regarded as indicating any particular intention. It is well known that repairs must usually be made when there is a change of tenants; that new tenants will usually demand more than tenants who are settled on the premises. The old lessee is benefited by the making of such repairs if the result is to secure a new tenant more quickly, or to obtain a higher rental than would otherwise be realized. Such repairs do not, therefore, cause a surrender. Where expensive and unnecessary repairs have been made, the question is more serious. Such action on the part of the landlord may make it appear that he has taken advan- [fol. 81] tage of the tenant's default to eliminate him entirely, and to make the premises a source of greater profit to himself. Moreover, the making of extensive alterations means that the premises must stand idle while these alterations are being effected, and that the loss to the tenant may be aggravated."

In the instant case, the loss to the landlord was not aggravated by the work done by the landlord. On the contrary, by making the premises rentable, the debtor's damages were mitigated. Nor can any inference be drawn from the Special Master's report that the repairs were not necessary for the protection and preservation of the property. The legitimate inference is all the other way.

**The rule in other states is the same: Trick v. Eckhouse, 145 N. E. 587 (restoration of hole in outside wall); Hickman v. Breadford, 179 Iowa 827; Breuckman v. Twibill, 89 Pa. St. 58; Gerhart Realty Co. v. Brecht, 109 Mo. App. 25; Higgins v. Street, 19 Okla. 45, Cf. Siller v. Dunn, 284 Pac. 232 (furniture store altered into a hotel).

The tenant's alterations had seriously damaged the building (cf. Kinney Realty Company v. Salmon, 106 N. J. Eq. 389; Agate v. Lowenbein, 57 N. Y. 604; Woolworth v. Nelson, 85 So. 449 (Ala.)); the landlord merely repaired or restored the damage.

A holding that making repairs necessary to restore premises to their original condition effects a surrender would nullify the New Jersey rule that a landlord may relet for the tenant's account, since the privilege is worthless unless the landlord may put the premises in rentable condition. In the case at bar it was obviously essential, in order to relet, to close up the common entrance and replace the party wall, for the building was not rentable except as an independent unit.

(B) A further hearing on the merits of the claim should not be required.

The claim was submitted to the Special Master on the one narrow issue as to whether a surrender had been effected [fol. 82] by re-entry and reletting, and on an agreed statement of the facts deemed relevant to that issue. No question was submitted to him as to whether a surrender had been effected by the repair, restoration or alteration of the premises, and no facts relating to any such question were included in the stipulations.

The Special Master, therefore, erred in basing any conclusion upon the fact that the landlord had filed a claim in the prior bankruptcy proceedings for the cost of restoring alterations made by the tenant. His report is entitled to no more weight than the stipulated facts justify.

In re Pittsburgh-Big Muddy Coal Co., 215 Fed. 703, 706;

In re Sullivan Condensed Milk Co., 291 Fed. 66, 68.

This Court not only went outside the stipulated facts but went even beyond the Special Master's report when it stated that "the evidence * * * showed that the landlord had made substantial changes."

A stipulation is designed to restrict issues or to settle disputed facts, or both, and it is binding, unless cause is shown for setting it aside. Brooklyn Mining Co. v. Miller, 227 U. S. 194, 201; United States v. Davison, 1 F. (2d) 465, 469, 470; Schmertz Wire Glass Co. v. Continuous Glass

Press Co., 216 Fed. 828; McNeill v. Town of Andes, 40 Fed. 45.

Counsel for the Trustee have not urged and cannot urge any valid reason for being permitted to avoid the effect of their stipulation or to introduce new evidence in support of a new issue. They cannot claim mistake, fraud or surprise—they were at all times entirely familiar with all the relevant facts, since they were also counsel for the trustee [fol. 83] in bankruptcy in the prior bankruptcy proceeding. The stipulations did not reserve to any party the right to introduce additional proof.

The present case should be compared with General Utilities & Operating Co. v. Helvering, 80 L. Ed. 174, in which the case was submitted to the Board of Tax Appeals upon one issue and an agreed statement of facts. The Circuit Court of Appeals reversed a decision in favor of the taxpayer, on an entirely new issue, in support of which it made certain inferences of fact in conflict with the stipulated facts. The Supreme Court reversed, saying (p. 177):

"Here the court undertook to decide a question not properly raised. Also it made an inference of fact directly in conflict with the stipulation of the parties and the findings, for which we think the record affords no support whatever. To remand the cause for further findings would be futile. The Board could not properly find anything which would assist the Commissioner's cause.

See also Helvering v. Salvage, 80 L. Ed. 356, and Compania General v. Collector, 279 U. S. 306. In the latter case, the Supreme Court held for the government on the grounds that the burden was on the taxpayer to establish facts showing the invalidity of the assessment, and the statement of facts agreed to was not sufficient to sustain such burden.

The burden of proving surrender is also on the party relying on surrender (see cases cited at pp. 45, 46 of our Brief), and that burden has not been met here.

Even in an action at law, where the Seventh Amendment is applicable, an appellate court will, upon a reversal of [fol. 84] a case submitted upon an agreed statement of facts, direct the entry of final judgment without remanding for a new trial. Thomas v. Matthiessen, 232 U. S. 221, 236; United States v. Illinois Surety Co., 226 Fed. 653, 664 (C. C. A. 7); Massachusetts Bonding & Ins. Co. v. Santee,

62 F. (2d) 724, 728 (C. C. A. 9); Maryland Casualty Co. v. Beebe, 54 F. (2d) 743, 746.

The appellant has been subjected to over a year of litigation before the Special Master, in the District Court and in this Court, at considerable expense, on a question of law raised by an agreed statement of facts, which question of law this Court has just determined in her favor, to wit: that a landlord in New Jersey may relet without effecting a surrender. And, as we have shown, even if all the facts referred to by the Special Master and by this Court, and all reasonable inferences which could be drawn therefrom, were proven on another trial, they would not establish a surrender as a matter of law.

This Court ought not to remand for a new hearing on the merits under such circumstances, but should reverse with instructions that the claim be allowed, subject to proof of the amount of damages, which is the only issue reserved by the stipulations.

In any event, it is clear that this Court should not affirm, without remanding for a new hearing on the merits, on the basis of an alleged fact not contained in the agreed statement of facts. If this appeal is not to be decided upon the single issue presented in the record and upon the facts as stipulated with reference to that issue, as we insist it should be, then, at the very least, the appellant is entitled to her day in court and an opportunity to establish the actual facts.*

[fol. 85] Wherefore, appellant respectfully prays this Honorable Court for a rehearing of the appeal herein.

Dated, April 14th, 1936.

City Bank Farmers Trust Company, by Mitchell, Taylor, Capron & Marsh, Its Attorneys and Solicitors. Of Counsel: Rollin Browne. Henry L. Glenn.

We hereby certify that the foregoing petition for a rehearing is presented in good faith and not for delay.

Rollin Browne, Henry L. Glenn, Attorneys and Solicitors for the Appellant.

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* We do not intend, by making this point, to concede that respondents have any right to a further hearing on the merits, or to enlarge the issue or to supplement their stipulations by further proof.

[fol. 86] UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

In the Matter of

UNITED CIGAR STORES COMPANY OF AMERICA, Debtor

CITY BANK FARMERS TRUST COMPANY, Assignee of Florence H. Bugbee, Appellant

IRVING TRUST COMPANY, as Trustee of the Estate of the Above-named Debtor, et al., Appellees

Before Manton, Augustus N. Hand and Chase, Circuit Judges

Rollin Browne, Esq., Henry L. Glenn, Esq., Attorneys and Solicitors for the Appellant.

Per CURIAM:

Petition for rehearing denied.

——— ———, ——— ———, Circuit Judges,

Filed May 21, 1936.

[fol. 87] UNITED STATES CIRCUIT COURT OF APPEALS, SECOND CIRCUIT

At a stated term of the United States Circuit Court of Appeals, in and for the Second Circuit, held at the United States Court House in the City of New York, on the 21st day of May, one thousand nine hundred and thirty-six.

Present: Hon. Martin T. Manton, Hon. Augustus N. Hand, Hon. Harrie B. Chase, Circuit Judges.

In the Matter of

UNITED CIGAR STORES COMPANY OF AMERICA, Debtor

CITY BANK FARMERS TRUST COMPANY, as Assignee, etc., Appellant

A petition for a rehearing having been filed herein by counsel for the appellant;

Upon consideration thereof it is

Ordered that said petition be and hereby is denied.

Wm. Parkin, Clerk.

[fol. 88] [Endorsed:] United States Circuit Court of Appeals, Second Circuit. In re United Cigar Stores Company of America. Order. United States Circuit Court of Appeals, Second Circuit. Filed May 21, 1936. William Parkin, Clerk.

[fol. 89] UNITED STATES OF AMERICA,
Southern District of New York:

I, William Parkin, Clerk of the United States Circuit Court of Appeals for the Second Circuit, do hereby certify that the foregoing pages, numbered from 1 to 88, inclusive, contain a true and complete transcript of the record and proceedings had in said Court, in the case of In the Matter of United Cigar Stores Company of America, Debtor; City Bank Farmers Trust Company as Assignee, etc., Appellant, as the same remain of record and on file in my office.

In testimony whereof, I have caused the seal of the said Court to be hereunto affixed, at the City of New York, in the Southern District of New York, in the Second Circuit, this 30th day of June, in the year of our Lord one thousand nine hundred and thirty-six, and of the Independence of the said United States the one hundred and sixtieth.

Wm. Parkin, Clerk. (Seal United States Circuit Court of Appeals, Second Circuit.)

[fol. 90] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed October 26, 1936

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted, and the case is assigned for argument immediately following No. 151.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

FILED
AUG 6 1936
CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. 260

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

CITY BANK FARMERS TRUST COMPANY, assignee of Florence H. Bugbee,
Petitioner,

—against—

IRVING TRUST COMPANY, as trustee of the estate of the above-named debtor, et al.,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF.

ROLLIN BROWNE,
HENRY L. GLENN,
Counsel for Petitioners.

MITCHELL, TAYLOR, CAPRON & MARSH,
Of Counsel.

THE COURT PRESS, N. Y. C.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

CITY BANK FARMERS TRUST COMPANY, assignee of Florence H. Bugbee,

Petitioner,

—against—

IRVING TRUST COMPANY, as trustee of the estate of the above-named debtor, *et al.*,

Respondents.

PETITION FOR A WRIT OF CERTIORARI

To the Honorable Chief Justice of the United States and Associate Justices of the Supreme Court of the United States:

Your petitioner respectfully prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Second Circuit in the above-entitled case, affirming an order disallowing a landlord's claim under Section 77B of the Bankruptcy Act (quoted *infra,* at p. 13) for "injury resulting from the rejection" of a lease by a trustee in bankruptcy in a bankruptcy proceeding

pending prior to the enactment of Section 77B, where reorganization proceedings under that section were subsequently instituted in such bankruptcy proceeding.

(A) SUMMARY STATEMENT OF MATTER INVOLVED

(a) Facts

Two stipulations of fact constitute the only evidence in the case (R. 19, 33):

Florence H. Bugbee, leased to the debtor (United Cigar Stories Company of America) premises situated in Trenton, New Jersey, for a term commencing April 1, 1926, and expiring March 31, 1946 (R. 23). On August 29, 1932, the debtor filed a voluntary petition in bankruptcy, was adjudicated a bankrupt and abandoned the premises. On November 11, 1932, Irving Trust Company, the trustee in bankruptcy of the debtor, rejected the lease and abandoned the premises. After rejection of the lease, the landlord relet various portions of the premises without notice to the debtor.*

On June 9, 1934, while the bankruptcy proceeding was still pending, the debtor filed in the bankruptcy proceeding, its petition under Section 77B, and on June 14, 1934, the District Court approved the petition as properly filed.

The landlord assigned her claim to the petitioner, agent for the Landlords' Protective Committee in these proceedings, and proof of claim (R. 3) for injury resulting from the rejection of the lease was duly filed by the petitioner, as such assignee.

---

* The Special Master, to whom the matter was referred for consideration and report, also found, *sua sponte*, that the landlord had filed in the bankruptcy proceeding "a claim for $1,980.99 for alleged expenditures in restoring a party wall and in closing up a common entrance in the demised premises" (R. 41), though the two stipulations of fact which constituted the only evidence in the case contain no reference whatever to the filing of such claim, or to such restoration.

Irving Trust Company, which had been appointed trustee of the estate of the debtor in the reorganization proceedings, objected to the claim on the ground that the lease, which contained no special covenant for damages or indemnity, had been terminated by the landlord's *reentering and reletting the premises* after rejection of the lease (R. 14).

(b) Rulings of the Courts Below

The Special Master held that Section 77B "could not and did not create any valid and legal claims against the debtor where none existed prior to the enactment of said Section", and that none existed at the time of the enactment of the statute, since the *reletting* of the premises by the landlord had effected a surrender of the lease under the New Jersey law. The Master therefore recommended that the claim be disallowed (R. 37), and his report was confirmed by the District Court (R. 49, 53).

The Court of Appeals affirmed, holding (R. 71) that (1) the injury resulting from rejection of a lease for which a claim is allowable under Section 77B must be "recoverable damages" to which the claimant would be entitled under the applicable state law, and that (2) it was impossible for the petitioner to show that the landlord had "sustained any damages from injury by the rejection of the lease" (R. 73), since, *although under the law of New Jersey the landlord's reentry and reletting of the premises alone had not effected a surrender of the lease,** a surrender had been effected by the landlord's restoration of the premises to the condition they were in at the commence-

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* The rule in New Jersey is different from the rule in New York and some other states. *Liskorsky* v. *Blau*, 114 N. J. L. 324; *Dolton* v. *Sickel*, 66 N. J. L. 492; *Banks* v. *Berliner*, 95 N. J. L. 267.

ment of the term.* A petition for rehearing was denied on May 21, 1936 (R. 75, 83).

(c) Questions Presented

(1) Is a landlord who, after rejection of his lease and prior to the enactment of Section 77B, resumed possession, restored the premises to their original condition, and relet, a "person injured by such rejection", within the meaning of Section 77B, even though under the applicable state law such acts effected a surrender of the lease by operation of law?

(2) If so, is there grave doubt as to the constitutionality of the statute in that respect?

(3) Did the Court of Appeals err in holding that a surrender had been effected because the landlord so restored the premises (in addition to resuming possession and reletting), when the question so decided was not raised by the objection to the proof of claim and the stipulations of fact on which the case was submitted did not mention that the premises had been restored?

(4) Did the landlord's restoration and reletting effect a surrender under the law of New Jersey?

(B) REASONS FOR GRANTING THE WRIT

(1) The question of the proper interpretation of the provisions of Section 77B relating to landlords'

* The Special Master had held that the landlord's reentry and reletting had effected a surrender. He had referred, of his own motion, to the landlord's filing of the claim for restoration merely as "showing that the Landlord, prior to the enactment of Section 77-B, by her reentry and reletting of the premises as aforesaid, considered that the lease [had] terminated and expired", because the entire basis of the claim, in the Special Master's view, was the expiration of the lease (R. 41). See the annexed brief, at p. 22, *infra*.

claims is an important question of federal law which has not been, but should be, settled by this Court.

This Court has in recent years repeatedly recognized the importance of the question of provability of landlords' claims in equity and bankruptcy proceedings (under the old Act), by reviewing on certiorari the following cases: *Miller* v. *Irving Trust Co.*, 296 U. S. 256 (1935); *Irving Trust Co.* v. *A. W. Perry, Inc.*, 293 U. S. 307; *Manhattan Properties, Inc.* v. *Irving Trust Co.*; *Brown* v. *Irving Trust Co.*, 291 U. S. 320; *Kothe* v. *R. C. Taylor Trust*, 280 U. S. 224; *William Filene's Sons Co.* v. *Weed*, 245 U. S. 597 (equity).*

It seems clear that Congress, in including in Section 77B the provisions relating to landlords' claims, intended to change to some extent the rules established by the cases cited. These provisions obviously were patterned upon similar provisions of the English Bankruptcy Acts,** the decisions under which furnish a guide in the interpretation of the new statute. Under the English Acts landlords' claims have uniformly been allowed without regard to the presence or absence of special covenants and without regard to the common law rule that reentry extinguishes the tenant's liability.***

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* Under these decisions, all landlords' claims were held non-provable under the old Bankruptcy Act, whether or not the lease contained a covenant of indemnity and whether or not the landlord reentered before or after the filing of the petition,—except a claim based on a lease containing a liquidated damage clause which became operative *ipso facto* upon the filing of the petition in bankruptcy, as in the *Perry* case, *supra*.

** For instance, paragraph (7) of Section 55 of the English Bankruptcy Act of 1883 (46 and 47 Vict. c. 52) provided:

> "Any person injured by the operation of a disclaimer [rejection] under this section shall be deemed to be a creditor of the bankrupt to the extent of the injury, and may accordingly prove the same as a debt under the bankruptcy."

See also English Bankruptcy Act of 1914, 4 and 5 Geo. V., c. 59.

*** *Ex parte Blake*, 11 Ch. Div. 572; *Ex parte Llynvi Coal & Iron Co.*; *In re Hide*, L. R. 7. Ch. App. 28; *Ex parte Leather Sellers' Co.*, 3 Morrell, 126 (Q. B. D., 1886).

How far Congress intended to go in introducing into the American system the innovation of permitting landlords to share in the assets of the bankrupt tenant urgently requires clarification.

The extent of the litigation which has already arisen in the lower courts over the correct interpretation of these new provisions is shown by the status of claims filed in these reorganization proceedings. 138 landlords' claims filed in these proceedings, totalling $6,185,000,* are now in various stages of litigation. The major question involved in most of these litigated claims is, as in the case at bar, whether termination of the liability of the debtor under the applicable state law, after the bankruptcy or after the rejection of the lease but prior to the enactment of Section 77B, defeats the claim under Section 77B.**

The decision of the Court of Appeals in the case at bar and its decision in *In re United Cigar Stores Co. of America* (*Caroline R. Kuehner and Frederick G. Fischer, as trustees, appellants; Grayson M.-P. Murphy, et al., as a Preferred Stockholders' Protective Committee, et al., cross appellants*), not yet reported (decided by the Court of Appeals on July 14, 1936), are inconsistent with respect to the effect to be given to the local law in determining the validity of a landlord's claim under Section 77B. In the case at bar

* This figure is taken from the trustee's second report on claims dated June 11, 1936 and reflects the three year rent "limitation" prescribed in the statute.

** In many of these cases the leases were not affirmatively rejected by the trustee in bankruptcy, but the landlords accepted assignments of the leases and sub-leases, if any, thus effecting express surrenders, and the landlords also released the debtor from liability under the leases, in some cases reserving their rights with respect to provable claims. In the case at bar no release was given by the landlord nor was any assignment of the lease or sub-leases made by the debtor; nor was there an express surrender of the lease. The decision of the Court of Appeals in the case at bar was that the restoration and reletting of the premises *after rejection* effected a surrender *by operation of law* under the law of New Jersey.

the court held that no claim was allowable under Section 77B unless a valid claim existed under the local law; in the *Kuehner* case the court held that the balance of the claim in excess of three years' rent was not allowable under Section 77B, although perfectly valid under the local law.

The *Kuehner* case also presented other important questions arising under the statute, and, as counsel for the landlords in that case, we expect to file a petition for a writ of certiorari, and the cross appellants may also file a cross petition. That case and the case at bar, arising in the proceedings of this one debtor, present an opportunity for this Court to consider all the more important and difficult questions arising under this new statute with respect to landlords' claims, such as:

(1) Must the rejected lease contain a special covenant for damages or indemnity; (2) if so, does a covenant obligating the tenant to indemnify against loss of future rents entitle the landlord to the present allowance of his claim; (3) what is the effect under the statute of the landlord's reentry after rejection; (4) if such reentry does not defeat the claim, notwithstanding that the tenant's liability is thereby terminated under the applicable state law, is there grave doubt as to its constitutionality in that respect;* (5) what is the effect under the statute if, in addition to reentering, the landlord restores the premises and relets to other tenants; (6) what is the proper method

* The report of the Special Master and the opinion of the District Court in the case at bar show that they were both influenced in their interpretation of the statute by grave doubts as to the constitutional power of Congress to make provision for landlords whose leases had already been terminated prior to the enactment of the statute. That the Court of Appeals was also influenced in this case by similar doubts is indicated by its subsequent opinion in *In re United Cigar Stores Co. (Kuehner and Fischer, appellants), supra* (see annexed brief, p. 20, *infra*).

of liquidation of a landlord's claim,—where the lease contains a covenant to indemnify against loss of future rents and where it does not; (7) to what extent must local rules of law be adhered to in determining the validity and amount of landlords' claims; (8) what is the proper interpretation of the provision of the statute "limiting" landlords' claims to an amount not in excess of three years' rent; and (9) if the statute was intended to cut off entirely the excess of the claim over the amount of three years' rent, for the benefit of the stockholders of the debtor corporation, is the statute to that extent unconstitutional?*

Thus, on the basis of the reorganization proceedings of this debtor, not to mention those of other chain store corporations now pending, it is of substantial importance that this Court should construe the landlord provisions of Section 77B in order that the lower courts may have the benefit of a guide in their decision of the many other cases now pending.

The questions involved in the reorganization proceedings of this debtor are certain to arise in reorganization proceedings of other chain store corporations.** Due to the many locations at which their business is conducted, landlords' claims are apt to consti-

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* A decision of many of these questions under Section 77B will also constitute a precedent with respect to the construction of Section 4 of the Act of June 7, 1934 (48 Stat. 911), which amended Section 63 (a) of the Bankruptcy Act by adding a provision for provability of landlords' claims in bankruptcy liquidation proceedings. The two provisions are substantially similar, as Judge Hand recognizes in his opinion in *In re United Cigar Stores Co.* (*Kuehner and Fischer, appellants*): "This is obvious in §63 (a) (7) and the language there is like that of §77B (b) (10)."

** The extent to which reorganization proceedings have been resorted to by chain store corporations is indicated by the following partial list of such corporations which are now in reorganization under Section 77B in the Southern District of New York alone: Schulte Retail Stores Corporation; D. A. Schulte Inc. of New York; D. A. Schulte, Inc. of Delaware; Huylers, Inc. of Delaware; Huyler's, New York; Schulco, Inc.; H. L. Green Co.; Bellcamp Stores, Inc.; Radio-Keith-Orpheum Corp.; Diamond Brothers Apparel Corp.; Steuben Taverns; Liberty Baking Corp.; Sunnydale Food Stores, Inc.; Highland Dairy Co.; Albrecht's Stores, Inc.

tute the most important and numerous class of claims against such corporations.*

The Court of Appeals itself has recognized, in its subsequent opinion in *In re United Cigar Stores Co. (Kuehner and Fischer, appellants)*, *supra*, the difficulty of construing the landlord provisions of Section 77B.** It is respectfully submitted that the most appropriate time for the construction of these provisions of Section 77B is now, before conflicts in decisions arise in the lower courts and before the confusion arises which existed under the old Bankruptcy Act and finally resulted in applications to this Court for writs many years after the question was first presented to the lower courts.

This Court has recently granted writs to review questions of construction of this new section of the Bankruptcy Act because of its novelty and the difficulty of construing it.***

Some of such corporations which are in reorganization under Section 77B in other districts are as follows: Burg Company (Minn.); H. Winer Co. (Boston); Pollyanna Stores, Inc. (Conn.); Grant Lunch Corp. (Newark, N. J.); Donahoe's Inc. (Pittsburgh, Pa.); Gross Stores, Inc. (Phila., Pa.).

In recently pending reorganization proceedings of two large corporations similar questions regarding landlords' claims were also presented, but such claims were disposed of by compromise: Paramount Publix Corp. (S. D. N. Y.) and J. G. McCrory Co. (S. D. N. Y.)

* 354 of the 481 proofs of claim filed in the reorganization proceedings of this debtor were landlords' claims, amounting to over $13,700,000 (limited to three years' rent) out of a total of all claims of approximately $20,000,000 (Trustee's First Report on Claims).

** Judge Learned Hand said: "It is very difficult to know what the section really means"; "the language is obscure".

*** Writs have been granted in the following cases involving questions under Section 77B:

Nettie Meyer, et al. v. *Kenmore Granville Hotel Company, et al.*, 296 U. S. 565 (whether appeal lies as a matter of right from an approval of a petition for reorganization); *C. S. Tuttle, et al.* v. *Sam Harris, et al.*, 296 U. S. 567 (whether pending foreclosure proceeding is a prior proceeding in an equity receivership); *Theodore Stitt* v. *Reconstruction Finance Corporation*, 296 U. S. 570 (Referee's compensation where proceeding in bankruptcy superseded by 77B proceeding); *Stephen Callaghan, et al.* v. *Reconstruction Finance Corporation*, 296 U. S. 570 (whether compensation for trustees in bankruptcy governed by Section 48, although proceeding superseded by 77B proceeding); *Duparquet Huot & Moneuse Co. et al.* v. *Frysinger Evans, et al.*, 296 U. S. 569 (whether state court foreclosure proceeding is "equity receivership pending" under Section

The decision in the case at bar practically nullifies the obvious attempt of Congress to make provision for landlords whose leases were rejected in bankruptcy proceedings pending at the time of enactment of Section 77B.* It is fair to assume that very few landlords whose leases had been rejected in bankruptcy proceedings prior to the enactment of Section 77B sat idly by and allowed the premises to remain vacant instead of resuming possession and reletting in order to minimize their losses, irrespective of the presence or absence of covenants for damages or indemnity in their leases and irrespective of the effect of reletting on the debtor's liability under the local law.

The extensive existing litigation in the instant proceedings, the probability of similar extensive litigation in the many other reorganization proceedings of chain store corporations now pending, the resulting probable conflict in the future between decisions of the various Courts of Appeal and the difficulty of effecting reorganizations of chain store corporations pending a final determination by this Court of the status of landlords' claims under Section 77B—all these considerations attest the importance of this question, which, notwithstanding the numerous decisions under the old Bankruptcy Act, remains almost as novel and confusing as ever to the courts and to the bar.

77B); *Baxter N. Foust* v. *Munson Steamship Lines*, 80 L. Ed. 746 (whether general restraining order includes pending tort suit although debtor covered by a liability insurance); *Tennessee Publishing Co.* v. *American National Bank et al.*, 80 L. Ed. 957 (whether reorganization plan was properly dismissed as unworkable).

* There can be no doubt that such provision was made in recognition of the known fact that many solvent corporations, particularly chain store corporations, had resorted to bankruptcy during the depression, solely or primarily for the purpose of ridding themselves of liability under their leases (42 Yale L. J. 1003; 33 Col. L. Rev. 231-4; 7 Univ. of Cinn. L. Rev. 164-5; see also the remarks of Representative Celler on the floor of the House, 76 Cong. Rec., Pt. 2, p. 1360, with regard to the debtor in the case at bar).

(2) A writ should also be granted because the Court of Appeals, in basing its affirmance on the landlord's restoration of the premises, when the pleadings and the proof raised no issue as to such restoration, has so far departed from the accepted and usual course of judicial procedure as to call for an exercise of this court's power of supervision and because the procedure of the Court of Appeals in this respect is probably in conflict with the decisions of this Court in *Liberty National Bank* v. *Bear,* 265 U. S. 365, 370-1 and *General Utilities & Operating Co.* v. *Helvering,* 296 U. S. 200, 206.

(3) Moreover, the decision of the Court of Appeals that the landlord could not restore the premises (in order to relet after the tenant's abandonment) without effecting a surrender is clearly in conflict with the applicable local decisions. *Zabriskie* v. *Sullivan,* 80 N. J. L. 673, 676, aff'd 82 N. J. L. 545; *Block* v. *Bell Furniture Co.,* 111 N. J. Eq. 551, 556, 559-561; *cf., Liskovsky* v. *Blau,* 114 N. J. L. 324; *Banks* v. *Berliner,* 95 N. J. L. 267; Schnebly, Operative Facts in Surrenders, 22 Ill. L. Rev. 117, 129. The two cases cited by the Court of Appeals (R. 73) in support of its conclusion to the contrary are not in point. While it cannot be said that this question of local law is of sufficient importance in itself to warrant the granting of a writ, the clear conflict between the decision of the Court of Appeals and the decisions of the New Jersey courts adds weight to the reasons for review already stated.

For the above reasons it is respectfully submitted that this petition should be granted.

CITY BANK FARMERS TRUST COMPANY,
assignee of Florence H. Bugbee,
By ROLLIN BROWNE,
HENRY L. GLENN,
Counsel for Petitioners.

BRIEF IN SUPPORT OF PETITION

OPINIONS BELOW

The opinion of the District Court (per Hulbert, *D. J.*) appears at page 49 of the record and is not officially reported, but is reported in C. C. H. Bankruptcy Law Service, par. 3702. The opinion of the Court of Appeals (per Chase, *C. J.*) is reported in 83 F. (2d) at page 209 and appears in the record at page 71.

JURISDICTION

Jurisdiction to issue the writs is vested in this Court by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925, c. 229, Sec. 1, 43 Stat. 938, 28 U. S. C. A. Sec. 347 (a). The order for mandate was entered April 13, 1936. A petition for rehearing, seasonably filed on behalf of the petitioners, was entertained by the Court of Appeals and denied by an order entered May 21, 1936 (R. 75, 83).

STATEMENT OF THE CASE

The facts, rulings of the courts below and questions presented are set forth in the foregoing petition.

STATUTE INVOLVED

Subdivision (b) of the Corporate Reorganizations Act (Section 77B of the Bankruptcy Act [48 Stat. 911]) reads in part as follows*:

> "In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding in-

* Other pertinent provisions of Section 77B are quoted *infra*.

stituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity, in a proceeding pending prior to the institution of a proceeding under this section any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor. The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63 (a) of this act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or reentry * * *."

SPECIFICATION OF ERRORS

The Court of Appeals erred in holding:

(1) that the petitioners' claim was not allowable because the liability of the debtor on the lease had been terminated under the applicable state law, after rejection of the lease but prior to the enactment of the statute, by the landlord's restoration of the premises and reletting;

(2) that a surrender had been effected by the landlord's restoration of the premises (in addition to resuming possession and reletting) when the question so decided was not raised by the pleadings or the proof;

(3) that the landlord's restoration and reletting did, under the law of New Jersey, effect a surrender and terminate the liability of the debtor; and

(4) in failing to reverse, with instructions to allow the claim, subject to determination of the amount thereof.

ARGUMENT

POINT I.

The Court of Appeals in misconstruing Section 77B has wrongly decided a new and important question of Federal Law.

The importance of the interpretation of the provisions of Section 77B relating to landlords' claims has been shown in the petition. The extensive litigation surrounding the allowability of landlords' claims under the new statute demonstrates that the status of such claims is even more confusing to the bar and to the courts than under the Bankruptcy Act prior to its amendment.

The conclusion of the Court of Appeals, that the continuing liability of the debtor under the rejected lease is a condition to the allowability of the landlord's claim for the injury sustained by the prior rejection of his lease, arose from a complete misconception of the nature of the *injury* which the statute intended to recognize. The injury suffered by the landlord whose lease is rejected in bankruptcy con-

sists merely in the circumstance that, instead of his lease being assumed and performed according to its terms as a liability of the bankrupt estate, the lease is rejected, the premises are abandoned and the landlord is remitted to the bankrupt corporation for the continued performance of the covenants of the lease. The continued liability of the bankrupt corporation on the lease is of no value and, therefore, of no significance in ascertaining the fact or the extent of such injury.

When the Court of Appeals stated that it was necessary for the injured landlord to prove "recoverable damages as a result of the rejection",* it overlooked the fact that *injury resulting from rejection of a lease in bankruptcy* is an injury which, prior to the enactment of Section 77B, was not known to American law** and gave the landlord no right to recover any damages whatever.

While we recognize that the exact terminology employed in Section 77B is novel and involves difficulties of interpretation, we submit that the opinion of the Court of Appeals in the case at bar and its opinion in the *Kuehner* case reflect a confusion as to the underlying purpose and scope of the statute which could have arisen only from its failure to familiarize

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* The court said in the case at bar (R. 72-3):

> "It was necessary for the appellant to prove recoverable damages as a result of the rejection";

and again: (R. 72):

> "Whether such a claim is allowable under Section 77B * * * depends upon whether, under the applicable state law, it is capable of proof on the merits."

In its opinion in the *Otis* case, the Court of Appeals said:

> "That section does not extend the liability of a lessee beyond what it otherwise would be under applicable law."

** A somewhat similar statute was enacted in Massachusetts many years ago, but apparently has never been squarely passed on by the courts. *Bowditch* v. *Raymond*, 146 Mass. 169.

itself with the English statutes on which the landlord provisions of Section 77B were patterned and the decisions thereunder (see the Petition, *supra,* p. 5).

The mere fact that the injured landlord was given a claim, not for the entire future rent, but only for his injury or damages establishes that it was the intent of Congress that the landlord should resume possession of the abandoned premises and relet them in order to mitigate his damages. Yet, although the law of New Jersey is otherwise (see *supra,* p. 3, footnote), in many jurisdictions reletting by the landlord automatically releases the tenant from further liability, in the absence of an express covenant in the lease continuing his liability after termination. However, the fact that the statute refers to a landlord's claim for injury resulting from rejection of his lease and, in the alternative, to a claim for damages or indemnity under a covenant contained in the lease, shows conclusively that the claim for injury from rejection does not depend upon the presence of a special covenant in the lease.

The decision of the Court of Appeals ignores the clear and unambiguous language of the statute and imposes conditions upon the allowability of landlords' claims which were never intended by Congress. Although many leases do contain special covenants expressly authorizing the landlord to relet the abandoned premises without releasing the tenant from liability, many leases do not contain such provisions. The decision of the Court of Appeals would prevent many landlords whose leases do not contain such special covenants from resuming possession of the premises and reletting them at current rental values, except at the sacrifice of their claims.

Under the decision in the case at bar the landlord would have had to allow the premises to remain idle from November, 1932, in order to preserve the claim under Section 77B, for he could not have relet without restoring the wall between the two buildings and he could not restore without effecting a surrender.

The decision of the Court of Appeals is likely to cause future uncertainty on the subject of allowability of landlords' claims in 77B proceedings. If after the rejection of a lease in a pending bankruptcy proceeding the landlords' re-entry and reletting prior to the enactment of Section 77B and the filing of the tenant's petition thereunder defeats the claim in a 77B proceeding, then the landlord's re-entry and reletting after the filing of the tenant's petition under Section 77B and the rejection of the lease by the reorganization trustee (where there has been no prior bankruptcy proceeding) and at any time before the end of the term or at least before the confirmation of a plan, would similarly be deemed to defeat the claim. The language of the opinion in the case at bar makes no distinction between rejection before the statute and rejection after the statute. Moreover, no distinction is made by the statute between a lease rejected by the trustee in the reorganization proceeding and one previously rejected by a bankruptcy trustee in a proceeding pending at the time of the institution of the 77B proceeding (see provision quoted *supra,* p. 13). In either case the "person injured by such rejection" is, without any qualification, "deemed to be a creditor" for the purpose of the plan and its *acceptance.*

Where the rejection occurred prior to the enactment of Section 77B in a bankruptcy proceeding still pending at the date of its enactment, and the tenant then filed its petition for reorganization in the bankruptcy proceeding, as the statute provides that it might do, the language making a person injured by

such prior rejection a creditor must mean a creditor of the *assets in the bankrupt estate* with which the debtor is revested upon the filing of the petition under Section 77B, which became in turn the reorganization estate. The fact that the injury referred to is that resulting from the release of such estate from liability for rent makes it clear that any action the landlord took in the interim which had the effect of terminating the liability of *the bankrupt corporation* on the lease is entirely immaterial.

The fact that reletting would release the bankrupt tenant under the law of some states was of no significance to landlords under the old Bankruptcy Act, for they could not share in the bankrupt estate under the old Bankruptcy Act and their rights against the bankrupt corporate tenant were worthless. Since Congress must have known that and in view of the absence of any distinction in the language of the statute between rejection prior to the enactment of the statute and rejection after the enactment of the statute, Congress must have intended that a reletting by the landlord prior to the enactment of the statute should not defeat the claim against the estate, no matter in what state the premises should be located.

This conclusion is confirmed by both the language and the legislative history of the statute. The landlord's claim is measured with reference to the date of "surrender of the premises to the landlord or * * * reentry of the landlord, whichever first occurs, * * * whether *before or after* the filing of the petition". Thus, it is clear that reentry before the filing of the petition for reorganization does not defeat the claim, although, under the law of many states, the landlord's reentry terminates the lease and releases the tenant from further liability.

Section 77B, as it originally passed the House, con-

tained a provision conditioning allowability of a landlord's claim upon his not having terminated the lease by reentry or otherwise. That provision was eliminated while the bill was pending in the Senate. (See H. R. 5884, 73rd Cong., 1st Sess., June 2, 1933 [p. 10]; 78 Congressional Record, 8109, 73rd Cong., 2nd Sess.; H. R. 5884, Print of May 7, 1934 [p. 11] H. R. No. 1821, 73rd Cong., 2d Sess. [p. 2]). The elimination of that provision, and the insertion in place thereof of the provision measuring the landlord's claim with reference to the date of his *reentry,* whether *before* or after the filing of the petition, clearly shows the actual intent of Congress that the claim should be allowed despite the termination of the lease, after its rejection, by reentry or other action of the landlord effecting a surrender by operation of law.

The intention of Congress as expressed in Section 77B and the contemporaneous amendment to Section 63 (a) was to change the rule of the *Manhattan Properties* case and provide for a new "division of the pot" of the tenant's estate in all bankruptcy proceedings pending at the date of the enactment of the Act of June 7, 1934 (a) in which the time for filing claims had not expired or (b) in which reorganization proceedings should thereafter be instituted. In neither case did Congress create a *substantive* right not theretofore existent. The leases were valid obligations of the landlord at the time of the institution of the original bankruptcy proceedings, and the statute merely corrected the injustice inherent in the former rule, so far as pending proceedings were concerned.

The Special Master (R. 39), the District Court (R. 50), and the Court of Appeals* were all influenced in

* Although the Court of Appeals made no reference in its opinion in the case at bar to its doubts as to the constitutionality, it is clear that it was influenced by such doubts because of the language used in its subsequent opinion on the claim of *Kuehner and Fischer, supra,* in which, in

their interpretation of the statute by their doubts as to the constitutional power of Congress to make provision for landlords whose leases had already been terminated.

Reference is respectfully made to the brief of *Amici Curiae* Godfrey Saxe and John Gerdes for a fuller discussion of the proper interpretation of the statute and of its undoubted constitutionality if construed as contended for.

POINT II.

The Court of Appeals, in deciding an issue not raised either by the pleadings or proof below, departed from the usual course of judicial procedure and decided a question of Federal procedure in conflict with the decisions of this Court.

As we have seen, the trustee's objection to the claim (R. 14) raised simply one narrow issue of local law,—to-wit, whether the landlord's *reentering and reletting* terminated the debtor's liability under the lease, no point having been made of the landlord's *restoration* of the premises to their former condition. Moreover, the stipulations of fact, which were drawn in the light of the sole issue raised by the trustee's objection, contained no reference whatever to the restoration of the premises or the filing of a claim for the expense thereof.

Even assuming that the Special Master had the right to take judicial notice of the landlord's filing

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speaking of a claim for "injury resulting from the rejection", it said: "But, whatever was meant, we cannot suppose that Congress was trying to make over the contract by imposing a liability for future rent on the lessee after the term had ended. Indeed, we should have considerable doubt whether the bankruptcy power would support such a method."

of a claim in the prior bankruptcy proceeding,* although not requested to do so by any party, the "finding" of the Special Master was simply that the landlord had filed a claim for the expense of restoration. His conclusion from this finding was that the filing of such a claim indicated that the landlord thought the lease had been terminated by her previous reentry and reletting because the debtor was under no obligation to restore until the expiration of the term.** He did not even consider whether the restoration itself was a factor bearing on the question of whether a surrender had been effected. He limited his report to the question raised by the objection to the proof of claim and the stipulated facts. The opinion of the District Court was similarly limited (R. 49).

The Court of Appeals, however, seized on the Special Master's "finding" that a claim for reimbursement of the expense of restoration had been filed and drew from it inferences of further facts,—to wit, that the repairs made by the landlord upon resuming possession were "structural changes" (R. 72), or "substantial changes in the premises" which were "indicative of the resumption of the dominion of them inconsistent with the continued status of landlord and tenant under the lease" (R. 73), and, by implication, that the repairs made by the landlord were not necessary for the preservation of the premises or in order to relet.

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* The Special Master's report (R. 41, fol. 123) states that "the stipulation herein shows that this claim [for restoration] is also asserted in this Reorganization proceeding", but the Special Master was mistaken in this respect, as the stipulations of fact upon which the case at bar was submitted (R. 19, 33) contain no reference to the filing of a claim for restoration either in the bankruptcy proceeding or in the reorganization proceeding.

** This conclusion, which was not approved by the Court of Appeals, was erroneous, since the claim was provable, if at all, only on the theory that the bankruptcy petition constituted an anticipatory breach of the agreement to restore. *In re Metropolitan Chain Stores*, 66 F. (2d) 485, 487; *Possart* v. *Irving Trust Co.*, 68 F. (2d) 807.

Under the law of New Jersey, the burden of proving facts showing a surrender rests on the party alleging surrender. *O'Neal* v. *Pearse*, 87 N. J. L. 382, aff'd 88 N. J. L. 733. If the trustee's objection had raised the issue that the landlord's action in making certain repairs had effected a surrender, the trustee would have been required to prove, or the petitioner could have caused to be inserted in the stipulation of facts, the details with respect to the repairs made by the landlord. As we shall show, if the record had definitely shown that the repairs made were necessary to preserve the premises or to make them rentable, the Court of Appeals must have held that no surrender had been effected (see *infra*, p. 25). All these considerations were ignored by the Court of Appeals when it decided this question without pleadings and without evidence, and without the Special Master's or District Court's having passed upon the question.

In thus proceeding, the Court of Appeals has ignored the elementary principles that appellate courts should limit their consideration of cases to issues properly framed and passed upon by the courts below, and to evidence regularly produced, and also has ignored applicable decisions of this Court. *Liberty National Bank* v. *Bear*, 265 U. S. 365; *General Utilities & Operating Co.* v. *Helvering*, 296 U. S. 200. See also *Helvering* v. *Salvage*, 297 U. S. 106 and *Compañia General* v. *Collector*, 279 U. S. 306.

This Court held in *Liberty National Bank* v. *Bear* that where neither the trustee's objection to a claim nor the proof introduced by it raises an issue of law, the Court of Appeals could not base its affirmance of an order disallowing the claim on such issue, but should have reversed. The trustee had objected to the claim on the ground that the judgment securing it

had been recovered within four months prior to bankruptcy, but had not alleged nor proved that the bankrupt was insolvent at that time. Similarly in the case at bar the trustee neither alleged nor proved the nature of the repairs made by the landlord nor alleged that the making of such repairs had effected a surrender.

See also the opinion of this Court in the *General Utilities & Operating Co.* case, *supra,* in which it was said (p. 206):

> "The second ground of objection, although sustained by the court, was not presented to or ruled upon by the Board. The petition for review relied wholly upon the first point; and, in the circumstances, we think the court should have considered no other. Always a taxpayer is entitled to know with fair certainty the basis of the claim against him. Stipulations concerning facts and any other evidence properly are accommodated to issues adequately raised."

POINT III.

The Court of Appeals, in holding that the restoration and reletting effected a surrender, has decided a question of local law contrary to the applicable local decisions.

Nothing in the record indicates that the restoration of the party wall and the closing up of the common entrance were not repairs which were required to preserve the building or to enable the landlord to relet the building as an independent unit for the account of the debtor. On the contrary, the only inference

that can be drawn from the report of the Special Master as to the nature of the repairs is that the debtor occupied the premises involved herein and the adjoining premises as one unit. Otherwise, the debtor would not have cut a common entrance nor have torn down the party wall between the two buildings. The further inference necessarily follows that Mrs. Bugbee, upon the debtor's default, was compelled to restore the party wall and close up the common entrance in order to prevent such injury as might otherwise result from the separate occupation of the adjoining premises either by the debtor or by a new tenant. The New Jersey decisions clearly hold that repairs made by a landlord upon his tenant's abandonment for the purpose of preserving the premises from injury do not effect a surrender of the lease, even when accompanied by reletting. *Meeker* v. *Spalsbury,* 66 N. J. L. 60; *Liskovsky* v. *Blau,* 114 N. J. L. 324; *Banks* v. *Berliner,* 95 N. J. L. 267; *Block* v. *Bell Furniture Co.,* 111 N. J. Eq. 551, 559.

Assuming, *arguendo,* that the repairs made by the landlord in the case at bar were not necessary to preserve the premises under the doctrine of these cases, it is clear that where the repairs made by the landlord go no further than to restore the premises to their original condition, the repairs so made do not effect a surrender, even when accompanied by reletting. *Zabriskie* v. *Sullivan, supra.* This rule appears to be of general application in states where reletting alone does not effect a surrender. 22 Ill. L. Rev. 117, 129, *supra.* Any other doctrine would nullify the New Jersey rule that a landlord may relet for the tenant's account (see cases cited *supra,* p. 3, footnote), since the privilege is worthless unless the landlord may put the premises in rentable condition. It is ap-

parent that the premises in the case at bar could not have been relet as an independent unit without four walls and their own private entrance, and that the landlord's repairs were necessary in order to enable her to relet. Neither principle nor common sense required the landlord to try to relet the premises to such new tenant as might ultimately lease the adjoining premises, even if that had been possible.

Respectfully submitted,

ROLLIN BROWNE,
HENRY L. GLENN,
Counsel for Petitioners.

MITCHELL, TAYLOR, CAPRON & MARSH,
Of Counsel.

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CHARLES ELMORE CROPLEY

IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. 260.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

CITY BANK FARMERS TRUST COMPANY,
assignee of Florence H. Bugbee,

Petitioner,

—against—

IRVING TRUST COMPANY, as trustee of the estate of the above-named debtor, *et al.*,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI.

PETITIONER'S REPLY BRIEF.

ROLLIN BROWNE,
HENRY L. GLENN,
Counsel for Petitioner.

MITCHELL, TAYLOR, CAPRON & MARSH,
Of Counsel.

THE COURT PRESS, N. Y. C.

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ON PETITION FOR WRIT OF CERTIORARI.

PETITIONER'S REPLY BRIEF.

The numerous inaccuracies and fallacies in the trustee's brief might, in the absence of a reply, mislead the Court:

I.

(1) The trustee's statement (p. 5) that the questions set forth on page 7 of the petition are merely questions that "*might* arise in the construction of the provisions for landlords' claims in Section 77B" is totally unjustified. The questions there set forth have *actually* arisen in the case at bar and in the *Kuehner* case, and all nine of such questions have actually been

presented to this Court by the petition in the case at bar and the petition in the *Kuehner* case* (except question "(2)", which will be presented only if the cross-petitioners in the latter case file a petition).

(2) It is totally misleading for the trustee to state (p. 6) that only seven claims aggregating about $125,000 in amount "would be affected by the granting of a writ" in the case at bar. Perhaps the trustee means that those are the only claims which involve the precise situation presented by this case without any distinguishing features. For instance, the Voight claim alone, presented by the *amici curiae,* amounts to over $200,000, and there are numerous other claims, as mentioned in the petition, which involve, among other questions, the same fundamental question as that here presented.

(3) The fact that the English bankruptcy acts expressly provide that rejection shall terminate the liability of the bankrupt as well as the trustee does not distinguish those statutes from Section 77B. If a claim is provable under Section 77B, the liability of the tenant is automatically terminated upon the confirmation of a plan (see subdivision (h), Section 77B).

(4) The trustee's explanation of the reason for the elimination from the House bill of the provision conditioning provability of a landlord's claim upon the failure to terminate by reentry or otherwise, is entirely unconvincing. It was not necessary to eliminate this provision in order to make it clear that a claim based on a covenant for damages or indemnity should be allowable, for a covenant for damages or indemnity is clearly not terminated by reentry. Indeed, reentry is a condition precedent to the effective operation of a covenant of indemnity. (*Cf. Manhattan Properties,*

* The *Kuehner* petition (Docket No. 354) was filed on September 10, 1936.

Inc. v. *Irving Trust Co.*, 291 U. S. 320, 328-9; *Wm. Filene's Sons Co.* v. *Weed*, 245 U. S. 597, 602.) Secondly, the elimination of the House provision conditioning allowability also clearly bore no relation to whether or not the provision for provability should be applicable to pending proceedings.

(5) In arguing that the construction contended for by it avoids grave question as to the constitutionality of the statute (p. 13), the trustee merely emphasizes the desirability of the issuance of a writ by this Court. Without arguing this question at the present time, it is sufficient to point out that *the trustee's position ignores that a valid lease was in existence at the time of the institution of the original bankruptcy proceeding in 1932,* and that the statute goes no further than to do away, for the purpose of the bankruptcy law, with the historical distinction between contracts relating to personalty and contracts relating to realty.*

II.

(6) The trustee states (p. 8) that the reentry, restoration, and reletting together terminated the lease "in accordance with its terms and under the applicable New Jersey law". It is significant that the trustee does not refer to any provision of the lease to that effect, or to any New Jersey decision.

(7) The trustee also states (p. 13) that the District Court held, following the Special Master, that the landlord's reentry "and her subsequent acts" terminated the debtor's liability under the lease, and that the "subsequent acts" were the "restoration of the

* Congress may in the exercise of its bankruptcy power, like its other plenary powers, impair or destroy contract rights or common law defenses, if the challenged provision bears a reasonable relation to the subject of bankruptcies. A provision conferring the character of provability on a claim clearly bears *such* a relation. *Cf. Norman* v. *B. & O. R. Co.*, 294 U. S. 240.

alterations" which the debtor had made and the reletting to other tenants. This is an incorrect statement of the District Court's holding. The District Court merely confirmed the Master's report and, as has been pointed out in the petition (p. 7) and our main brief (p. 22), the Special Master held that the action of the landlord in reentering and reletting without notice to the tenant terminated the lease, the Special Master adding that the fact that the landlord filed a claim for the cost of restoring the premises showed that "*by her reentry and reletting* of the premises as aforesaid, [she] considered that the lease terminated and expired" (R. 41).*

Since the Master, the referee in the prior bankruptcy proceedings, must be presumed to have known all the facts regarding the restoration, it is highly significant that the Master did *not* find that the repairs and restoration made by the landlord were of such nature as to change the character of the premises and thus effect a surrender by operation of law, irrespective of the intention of the landlord.** The duty of the Court of Appeals was, if not to reverse, to send the case back to the Master, not "in order for the Trustee to plead a fact as to which there was no dispute", but to enable the parties to introduce proof as to the exact nature of the repairs to be

---

* The Master did not find that "the alterations made by the debtor had in fact been restored by the landlord", as the trustee asserts, nor "the facts with regard to the restoration" (pp. 16, 17). The petitioner's exception (R. 44, par. 5) was fully as broad as the "finding" of the Master.

** The filing of the claim for restoration did not evidence the landlord's understanding that the lease had been previously terminated, as the theory of the claim was that the bankruptcy had operated as an anticipatory breach of the covenant to restore (main br., p. 22n). That this was the theory of the claim is shown by the allegation in the proof of claim that "the lease has now expired *by reason of the bankruptcy*".

pleaded* and to enable the Master and the District Court to pass upon the legal question as to whether the making of such repairs effected a surrender by operation of law, a question which neither had passed upon.**

(8) The trustee also states (pp. 16, 18) that the landlord was "free" to restore the debtor's alterations only at the "expiration or other determination of the lease". The trustee refers to a covenant of the lease appearing on page 28 of the record in support of this assertion. The provision referred to merely provides that if the lessee should make any *improvements upon the premises*, "said improvements" should become the property of the landlord at the expiration or other determination of the lease. Obviously a *removed* party wall and a *hole in another wall* were not improvements which could become the property of the landlord at any time.***

Respectfully submitted,

ROLLIN BROWNE,
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Counsel for Petitioner.

MITCHELL, TAYLOR, CAPRON & MARSH,
Of Counsel.

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* *E. g.*, whether the repairs were required to preserve the building or to enable the landlord to relet it as an independent unit.

** General Order in Bankruptcy XLVII has no relevancy to a situation where the record is insufficient to enable the appellate court to determine whether the Master's conclusion was right, for a different reason than that relied on by the Master.

*** Even if they could be deemed improvements, the provision would clearly be inapplicable where the debtor *abandoned* the premises and the so-called improvements, as the debtor and the trustee did in the case at bar. In any event it would not follow that restoration of the *premises* (not of the alterations, as the trustee phrases it) would effect a termination of the lease under its terms. The only result would be the liability of the debtor for conversion of the improvements.

DEC 4 1936
CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. 260.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

CITY BANK FARMERS TRUST COMPANY, assignee of Florence H. Bugbee,
Petitioner,

against

IRVING TRUST COMPANY, as trustee of the estate of the above-named Debtor, *et al.*,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR PETITIONER.

HENRY L. GLENN,
Counsel for the Petitioner.

ROLLIN BROWNE,
RALPH MONTGOMERY ARKUSH,
MITCHELL, TAYLOR, CAPRON & MARSH,
Of Counsel.

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Respondents.

BRIEF FOR PETITIONER.

OPINIONS BELOW.

The only opinion below officially reported is that of the Circuit Court of Appeals for the Second Circuit, which is reported in 83 F. (2d) at page 209. The District Court opinion appears in the record at page 49.

JURISDICTION.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925. The order for mandate of the Court of Appeals was entered April 13, 1936 (R. 74). The petitioner's petition for rehearing was denied by the Court of Appeals by an order entered May 21, 1936 (R. 75, 83). The petition for certiorari was filed August 6, 1936, and granted October 26, 1936.

STATEMENT OF THE CASE.

This case involves the allowability in proceedings under Section 77B of the Bankruptcy Act of the claim of a landlord "for injury resulting from the rejection" of her lease prior to the enactment of Section 77B by the trustee of the debtor's estate in a bankruptcy proceeding in which reorganization proceedings subsequently were instituted.

(a) *Facts.*

The petitioner's assignor, Florence H. Bugbee,[1] leased to the debtor, United Cigar Stores Company of America, premises situated in Trenton, New Jersey, for a term commencing April 1, 1926, and expiring March 31, 1946 (R. 23). On August 29, 1932, the debtor filed a voluntary petition in bankruptcy, was adjudicated a bankrupt, and abandoned the premises. At the time of bankruptcy a portion of the premises had been sublet by the debtor. On November 11, 1932, Irving Trust Company, the trustee in bankruptcy of the debtor, rejected the lease and abandoned the premises. After rejection of the lease, the landlord, without notice to the debtor, relet various portions of the premises to the subtenants in possession, and later let certain portions to new tenants (R. 19, 33).

No release or assignment agreement such as is involved in *Meadows* v. *Irving Trust Co.* (No. 151) or in *Otis* v. *Irving Trust Co.* (No. 436), or of any other kind, was executed by the landlord at any time.

---

[1] Florence H. Bugbee assigned her claim against the debtor to the petitioner as Agent for the Landlords' Protective Committee in these proceedings.

On June 9, 1934, while the bankruptcy proceeding of the debtor was still pending, the debtor filed its petition under Section 77B in such bankruptcy proceeding, as permitted by the statute.

The petitioner in due course filed a proof of claim (R. 3) for injury resulting from the rejection of the lease. Irving Trust Company, which had been appointed trustee of the estate of the debtor in the reorganization proceedings, objected to the claim on the ground that the lease, which contained no special covenant for damages or indemnify, had been terminated by the landlord's *reentering and reletting the premises* after rejection of the lease (R. 14).

Although the two stipulations of fact which constitute the only evidence submitted to the Special Master, to whom the claim was referred by the District Court for consideration and report, do not contain any reference to the landlord's restoration of the premises prior to reletting, or to her filing of a claim in the prior bankruptcy proceeding for the expense of such restoration, the Special Master, *sua sponte*, stated in his report (R. 41) that the landlord had *filed* in that bankruptcy proceeding "*a claim* for $1,980.99 for alleged expenditures in restoring a party wall and in closing up a common entrance in the demised premises".

(b) *Statute Involved.*

The pertinent provisions of the Corporate Reorganizations Act, which was added to the Bankruptcy Act as Section 77B thereof by the Act of June 7, 1934, 48 Stat. 911, are:

Subdivision (a):

> "Any corporation which could become a bankrupt under Section 4 of this Act, * * * may file an original petition, * * * in any proceeding pending

in bankruptcy, whether filed before or after this section becomes effective, * * *."

Subdivision (b) (10):

"* * * The term 'creditors' shall include for all purposes of this section and of the reorganization plan, its acceptance and confirmation, all holders of claims of whatever character against the debtor or its property, including claims under executory contracts, whether or not such claims would otherwise constitute provable claims under this Act. The term 'claims' includes debts, securities, other than stock, liens, or other interest of whatever character. * * *

"In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity, in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor. The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63(a) of this Act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or reentry: * * *"

Subdivision (p):

"This section shall take effect and be in force from and after the date of the approval of this amendatory Act and shall apply as fully to debtors, their stockholders and creditors, whose interests or debts have been acquired or incurred prior to such date, as to debtors, their stockholders and creditors, whose interests or debts are acquired or incurred after such date. Proceedings under this section may be taken in proceedings in bankruptcy which are pending on the effective date of this amendatory Act."

(c) *Rulings of the Courts Below.*

The Special Master recommended that the claim be disallowed (R. 37) on the ground that Section 77B "could not and did not create any valid and legal claims against the debtor where none existed prior to the enactment of said Section", and that none existed at the time of the enactment of the statute because the landlord's *reentry and reletting* of the premises had effected a surrender of the lease under the New Jersey law. The master's report was confirmed by the District Court (R. 49, 53).

The Court of Appeals affirmed the disallowance of the claim, holding (R. 71) (1) that injury resulting from rejection of the lease for which a claim is allowable under Section 77B must be "recoverable damages" to which the claimant would be entitled under the applicable state law, and (2) that it was impossible for the petitioner to show that the landlord had "sustained any damages from injury by the rejection of the lease" because, *although under the law of New Jersey the landlord's reentry and reletting of the premises alone had not effected a surrender of the*

lease,[1] a surrender had been effected by the landlord's restoration of the premises to the condition they were in at the commencement of the term.[2]

(d) *Questions Presented.*

(1) Was the petitioner's assignor a "person injured" by the rejection of her lease within the meaning of Section 77B, and is the petitioner's claim accordingly provable herein, whether or not under the applicable state law the restoration of the premises and reletting effected a surrender of the lease before the enactment of Section 77B.

(2) Upon abandonment of the premises by the debtor, did the restoration of the premises "to the condition they were in when leased" and reletting by the landlord without notice to the debtor effect a surrender under the law of New Jersey?

(3) If so, did the Court of Appeals nevertheless err in so holding when the stipulations of fact on which the case was submitted did not mention that the premises had been restored and the question as to the effect of the restoration was not raised by the trustee's objection to the proof of claim?

SPECIFICATION OF ERRORS.

The Court of Appeals erred:

(1) In holding that the petitioner's claim was prop-

[1] The rule in New Jersey in this respect is different from the rule at common law and that in effect in New York and some other states (see *infra*, p. 45).

[2] As the statement of facts, *supra*, states, the record did not show that the landlord had restored the premises prior to reletting. *Even the Master's report did not state that the landlord had restored the premises* (R. 41). Moreover, as stated, the trustee's objection to the claim had raised no issue as to restoration.

erly disallowed because the debtor's liability on the lease had been terminated by a surrender under the applicable state law prior to the enactment of Section 77B;

(2) In holding that the debtor's liability on the lease had been terminated under the law of New Jersey by the landlord's restoration and reletting of the premises after their abandonment by the debtor;

(3) In basing its affirmance on the landlord's restoration of the premises when neither the pleadings nor the proof raised any issue as to such restoration; and

(4) In failing to reverse, with instructions to allow the claim in the amount of any loss that should be proved to have been incurred.[1]

SUMMARY OF ARGUMENT.

The petitioner's claim is allowable whether or not under the applicable state law the lease was terminated by the landlord's restoration and reletting after rejection in the prior bankruptcy proceeding but before the enactment of Section 77B. The language and the background and legislative history of the statute make it clear that Congress intended to grant relief to all landlords whose leases were previously rejected, entirely irrespective of whether or not their reoccupation or reletting of the premises terminated their leases under the technical law of landlord and tenant of the respective states. From the practical

[1] The two stipulations of fact (R. 19, 33) reserved for future determination the question of the amount of the damages suffered in the event that the claim should be held to be provable.

point of view, such action on the part of landlords had the effect of simply mitigating their loss.

The meaning of the statute is so clear that supposed doubts as to its constitutionality cannot possibly influence its construction. Besides, there are not sufficient doubts as to its constitutionality to influence its construction.

But whether or not the statute is construed in the manner mentioned, the petitioner's claim is allowable, since under the law of New Jersey the liability of the debtor on the lease survived restoration and reletting of the premises.

Finally, since the Court of Appeals committed reversible error in affirming on the ground that the landlord restored the premises, when no issue as to *restoration* was raised either by the pleadings or the proof, in the view of the case least favorable to the petitioner there must be a reversal with instructions for a new trial.

POINT I.

The petitioner's claim is allowable, whether or not under the applicable state law the lease was terminated by the landlord's restoration and reletting after rejection but before the enactment of Section 77B.

As we shall show, the liability of the debtor on the lease did not terminate under the New Jersey law. But if we are wrong in this contention and the debtor's liability is held to have been terminated, it will be because of the trifling and fortuitous circumstances that the landlord, in order to put the premises in a rentable condition, restored a wall and closed a common entrance. Those two acts, according to the

decision below, deprived her of the right to participate in the reorganization of the debtor.

It would seem that a conclusion based on so narrow a ground would have resulted only from a compelling reason such as a clear mandate in the wording of the statute or a plain legislative intent found in the background or history of the enactment. On the contrary, as we shall presently show, that background, history and text clearly require the opposite conclusion. Before doing so it may be helpful to point out what would have been the situation if the landlord had not restored the wall and closed the common entrance.

If perchance when the trustee in bankruptcy rejected her lease the premises had been entirely sublet, she could, according to the court below, have collected the subrents and would still be entitled to prove a claim. *In re Paramount Publix Corp.* (*Madison-Toledo Co.* v. *Paramount Pictures, Inc.*), 85 F. (2d) 83. If, at the time of rejection, the premises had not been sublet and the landlord had reentered and relet the premises without restoring the wall and entrance, she would, according to the opinion below, be entitled to prove a claim. So, merely the fortuitous circumstances that the premises were not entirely sublet and that it was necessary to make some restoration in order to relet them have placed the landlord outside the pale of persons to be benefited, though the result of her acts as a practical matter merely served to mitigate her damages and establish the present rental value of the property.

That, far from intending any such result, Congress intended to give a standing in reorganizations under Section 77B to all landlords who had been injured by the epidemic of tenant bankruptcies, irrespective of

any intricacies and technicalities of real estate law in forty-eight different jurisdictions is clearly apparent from the background, history, and language of the enactment.

(a) *Background and Legislative History of the Statute.*

Under the decisions of this Court, no landlord's claim for damages for loss of future rent was provable under the Bankruptcy Act as it existed prior to its amendment by the Act of June 7, 1934, except a claim based on a lease containing a liquidated damage clause which became operative before or *ipso facto* upon the filing of the tenant's petition in bankruptcy. *Manhattan Properties, Inc.*, v. *Irving Trust Co.*, 291 U. S. 320; *Miller* v. *Irving Trust Co.*, 296 U. S. 256; *Kothe* v. *R. C. Taylor Trust*, 280 U. S. 224; *Irving Trust Co.* v. *A. W. Perry, Inc.*, 293 U. S. 307.

Landlords' claims were held non-provable because too contingent. The contingent character of such claims resulted from the applicability to such claims of the law of landlord and tenant instead of the doctrine of anticipatory breach ordinarily applied to executory contracts relating to personalty. The latter doctrine not being applicable, the landlord had no cause of action for *damages* as for an entire breach, and the amount of the tenant's liability for *future rent* was uncertain in view of the fact that reentry under the general law of landlord and tenant in effect in the various states had the effect of terminating the tenant's liability for rent.

This doctrine of non-provability of landlord's claims under the old Bankruptcy Act was taken advantage of by chain store corporations which were desirous of ridding themselves of obligations under burdensome leases, to such an extent as to become almost a national scandal. Smith, Chain Stores and the Lease

Plague (1932), 58 Financial World, 367; Douglas and Frank, Landlords' Claims in Reorganizations, 42 Yale L. J. 1003; Schwabacher and Weinstein, Rent Claims in Bankruptcy, 33 Col. L. Rev. 213-4; 7 Univ. of Cinn. L. Rev. 164-5. These corporations sought bankruptcy not for liquidation but for reorganization.[1] The members of Congress must have been familiar with this general situation. Indeed, the attention of the members of the House was called to it by Representative Celler in January, 1933, on the floor of the House (76 Cong. Rec., Pt. 2, p. 1360).[2]

The old rule of non-provability obviously was not adapted to a bankruptcy statute which had as its aim reorganization instead of liquidation for, if the claim were not provable, the statute could not constitutionally discharge the reorganized company from its obligations under the lease. Accordingly, Section 77B as first passed by the House provided for provability of landlords' claims in the following language (H. R. 5884, 73d Cong., 1st Sess., Print of June 2, 1933, p. 10):

> "In case any executory contract shall be rejected, the same shall be deemed to have been breached and the holder shall be entitled to file a claim for damages for such breach and such claim may be allowed *provided such contract shall not have been terminated by forfeiture, reentry or otherwise.*" (Italics supplied throughout this brief unless otherwise stated.)

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[1] While landlords were entitled to the protection of the rule in *Northern Pac. R. R. Co.* v. *Boyd*, 228 U. S. 482, various methods of circumventing the rule were available in the absence of a vigilant and well financed opposition.

[2] Mr. Celler said, among other things, that the debtor in the case at bar was one of the solvent chain store corporations that had resorted to bankruptcy for such purpose. Although the record is silent with respect to this subject, it is significant that the debtor filed a voluntary petition under Section 77B two days after it was enacted.

The intent of this provision apparently was to make applicable to leases the doctrine laid down by this Court in *Central Trust Co.* v. *Chicago Auditorium*, 240 U. S. 581, with reference to executory contracts other than leases,—that is, to make the filing and approval of a petition under that bill followed by rejection of the lease an anticipatory breach for which *damages* could be proved. However, (1) the provision was applicable only to a *rejection after the enactment of the bill;* and (2) termination of the lease by the landlord by reentry or otherwise *prior to the hearing on his claim* would defeat the claim even though the termination should not occur until after such a rejection.[1] The effect of the *provision in the House bill, therefore, would have been to bar landlords who had terminated their leases by reentry or otherwise prior to the enactment of the bill* (or who should terminate thereafter but prior to hearings on their claims), and to enhance the amount of claims of landlords who did not terminate before the date of hearings on their claims, to the extent of the rent accruing in the period intervening between rejection and allowance of the claim.[2]

The unreasonableness of such a provision was apparent to the Senate Committee on the Judiciary, and upon its recommendation the Senate on May 2, 1934, amended the provision by substituting in place

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[1] Naturally read, the proviso clause limits the clause "and such claim may be allowed".

[2] Even under the provision of the House bill, however, termination of the lease by the landlord *after* the allowance of his claim would not have resulted in a subsequent disallowance. Aside from the many other reasons mentioned *infra* in discussing the effect of the provision as finally enacted, which are equally applicable to this provision, this is clear from the fact that the proviso clause itself refers only to termination *prior* to allowance of the claim,—"*shall not have been* terminated".

thereof (78 Cong. Rec. 8109) a provision reading substantially the same (so far as now material) as the form in which 77B was enacted, which is as follows:

> "In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor."[1]

This provision differs from the provision in the House bill in that the former is expressly applicable to rejection *prior to the enactment of the statute* and does not contain the proviso clause conditioning allowability upon failure to terminate prior to the date of the hearing on the claim (see discussion *infra*, pp. 32, 21). The only reasonable inference deducible from this legislative history is that under the provision as enacted the date of rejection in a prior bankruptcy proceeding is made the effective date of the anticipatory breach of the lease and that termination of the lease thereafter, whether by reentry or surrender by operation of law, is entirely immaterial.[2]

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[1] Section 63(a), which defines the claims which are provable in ordinary bankruptcy proceedings, was also amended by the Act of June 7, 1934, to make landlords' claims provable to a limited extent (48 Stat. 923).

[2] In its brief in opposition to the petitioner's application for certiorari (Appendix B thereof), the trustee argued that the provision in the House bill had to be discarded because (1) the effect of the proviso clause might have been to bar a claim based on a covenant for damages or indemnity, and (2) "the original

(b) *Rejection After Section 77B.*

Since the person made a creditor by the rejection provision of 77B is one *injured* by a rejection either before or after the enactment of the statute, without any distinction between the two, a brief consideration of the meaning and effect of the provision as applied to rejection after the enactment of the statute cannot fail to be of assistance in determining its meaning and effect as applied to a rejection prior to its enactment.

The landlord provisions of Section 77B obviously were patterned on the English bankruptcy acts [32 and 33 Vict., c. 71, Sec. 23 (1869); 46 and 47 Vict., c. 52, Sec. 55(7) (1883); 4 and 5 Geo. V, c. 59, Sec. 54(8) (1914)]. The language of Section 77B and of the provisions of the English Acts is almost identical,[1]

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phrasing was wholly inapplicable to pending bankruptcy or equity receivership proceedings."

But it was, of course, not necessary to eliminate the proviso clause in order to make it clear that a claim based on a covenant for damages or indemnity should be allowable, for such a covenant clearly is not terminated by reentry. Indeed, reentry is generally a condition precedent to the effective operation of such a covenant *Cf. Manhattan Properties, Inc.* v. *Irving Trust Co., supra; William Filene's Sons Co.* v. *Weed,* 245 U. S. 597. Secondly, making the provision expressly retroactive, rather than dispensing with the necessity of retaining the proviso clause, made its retention even more necessary if the intention was to bar a claim such as that in the instant case.

[1] Landlords' claims were first made provable by the English Bankruptcy Act of 1869. See *Manhattan Properties* case, *supra,* at page 332. The provision in that act was as follows:

> "Any person injured by the operation of this section [by a disclaimer, the English equivalent of a rejection] shall be deemed a creditor of the bankrupt to the extent of such injury, and may accordingly prove the same as a debt under the bankruptcy."

The provision in the English Act of 1883 and in the English Act of 1914 reads substantially the same.

except that the first English Act was not applicable to a rejection prior to its enactment.

The English courts have held that a landlord is "injured" by a disclaimer [rejection] if the fair rental value of the premises at the time the landlord repossesses them is less than the rent reserved in the lease, even in the absence of a covenant of indemnity or other special covenant for liability surviving termination of the lease, although under the English law the landlord could not recover damages in a lump sum against a solvent tenant; and that, accordingly, he has a claim provable in the bankruptcy proceeding to the extent of such difference. Not only is the provability of the claim not defeated by reletting by the landlord after the disclaimer, but the reletting is contemplated and the rent payable upon reletting is accepted as evidence of the fair rental value of the premises in the computation of the amount of the claim. *Ex Parte Blake*, 11 Ch. Div. 572; *Ex Parte Llynvi Coal & Iron Co., In re Hide*, L. R. 7 Ch. App. 28; *Ex Parte Leather Sellers Co.*, 3 Morrell 126 (Q. B. D. 1886); *Ex Parte Corbett*, 14 Ch. Div. 122 [1880]; *Ex Parte Walton*, 17 Ch. Div. 746 [1881]; *In re Hyams*, 93 L. J. Ch. 184 [C. A. 1923]; *Hardy* v. *Fothergill*, L. R. 13 App. Cas. 351 (House of Lords, 1888); *In re Carruthers*, 15 Reports 317, 2 Manson 172 (1895).[1]

[1] In an attempt to distinguish the English precedents the trustee in its brief in opposition to the granting of a writ (p. 10) relied on the provision in the English Act of 1869 (Sec. 23) that a disclaimed lease should "be deemed to have been surrendered" on the date of the order of adjudication, and in the English Act of 1883 [Sec 55(2)] and Act of 1914 [Sec. 54(2)] that disclaimer shall operate to determine the interest of the bankrupt as well as the trustee. The absence of these provisions in Section 77B, however, does not signify that termination of the lease under the state law after rejection has the effect of defeating the claim. If the claim is allowable, termination after rejection is

Under the test laid down in the instant case by the Court of Appeals (which, so far as can be determined from the language of its opinion makes no distinction between rejection before the statute and rejection after the statute) the claim is not allowable under Section 77B unless "under the applicable state law, it is capable of proof on the merits" (R. 72).[1] If this test should be applied literally, no landlord's claim would be provable under Section 77B, for neither the common law nor statute law of any state confers on the landlord a right of action against the tenant for *damages* in a lump sum for the loss which the landlord might suffer over the entire balance of

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contemplated even in the absence of an express provision providing that rejection shall terminate the interest of the bankrupt. A final decree in a proceeding under Section 77B releases the tenant from liability for future rent, so that the rejection plus the final decree has the effect of terminating the lease under that statute. Thus, the express provision in the English acts that adjudication or rejection shall terminate the lease, would, if contained in Section 77B, be material only in the event that proceedings were subsequently dismissed before final decree.

[1] In other places in its opinion the Court of Appeals reiterated the same thought in other language: "Section 77B makes such a claim provable provided there is evidence in support of it which constitutes proof as a matter of law" (R. 73). And again (R. 73-4): "It was necessary for the appellant to prove recoverable damages as a result of the rejection." "It therefore has no claim susceptible of proof as a matter of law" (R. 74). As the Court of Appeals expressed it in its opinion in these proceedings on the appeal of *Otis Estate Land Trust*, 83 F. (2d) 202, 206:

> "* * * It is necessary to have a claim against a debtor which the substantive law of landlord and tenant recognizes as an enforceable claim in order to have a provable claim under Section 77B. That section does not extend the liability of a lessee beyond what it otherwise would be under applicable law. *If under such law a landlord would have a claim against a lessee for damages or indemnity under a covenant contained in a lease which would have been recoverable in a civil action had there been no 77B petition approved, such claim may be proved* in the 77B proceedings and allowed to the limited extent above indicated."

the term. Apparently the Court of Appeals did not intend this test to be taken literally, for in its subsequent decision in *In re United Cigar Stores Co. (Kuehner and Fischer, Appellants)*, 85 F. (2d) 35, it held provable a claim of a landlord under a rejected lease which contained a covenant obligating the tenant to indemnify the landlord against loss of rent.

Clearly the "rejection" provision of Section 77B was not intended to be limited to claims based on leases which contain covenants for liquidated damages or indemnity. For, the reference in the limitation provision immediately following the rejection provision (see *supra*, p. 4) to a "claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate *or* for damages *or* indemnity under a covenant contained in such lease", shows conclusively that a claim "for injury resulting from the rejection" does not depend upon the presence of a special covenant in the lease.

This was recognized subsequently by the Court of Appeals in its decision in *In re Paramount Publix Corp. (Madison-Toledo Co.* v. *Paramount Pictures, Inc.)*, *supra*, in which it held provable a claim based on a rejected lease without a covenant for damages or indemnity (which had not been terminated prior to the enactment of the statute). It is implicit from the decision of the court, though it was not discussed, that termination of the lease before the confirmation of the plan would not defeat the claim.

In some respects this is even clearer under Section 77B than under the provisions of the English Acts:

(1) The claim is "limited" with reference to the date of termination of the lease: The limitation provision

immediately following the "rejection" provision provides:

> "The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity * * *, but shall be limited to an amount not to exceed the rent * * * for the three years next succeeding *the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after the filing of the petition,* plus unpaid rent accrued up to such date of surrender or reentry: * * *."

Thus the parity portion of the claim for injury resulting from the rejection is measured with reference to surrender of the premises to the landlord *or* reentry by the landlord. While "surrender" as here used apparently does not refer to a technical surrender of the leasehold estate, reentry (the date of which is controlling when reentry by the landlord precedes surrender) is a technical term denoting an act which puts an end to the leasehold estate. That Congress intended the word "reentry" to have its ordinary meaning is shown by its failure to use the expression "repossession of the premises by the landlord" in juxtaposition to "surrender of the premises to the landlord".

(2) The landlord's claim being for damages and not for future rent, the statute contemplates termination of the lease after rejection: Whatever else the limitation provision may mean, the legislative intention is clear that the claim shall not be allowed in an amount in excess of the total loss which it is estimated the landlord will suffer, where such total loss is less than the amount of three years' rent. No way of es-

timating the landlord's loss over the remainder of the term has ever been suggested other than the difference between rent reserved, discounted, and the fair rental value of the premises for the remainder of the term.[1] Allowability thus contemplates subtraction of the fair rental value of the premises in calculating damages. *Crediting the rental value of the premises contemplates use of the premises by the landlord for the purpose of reletting.* Occupation of the premises by the landlord; or reletting (in many states), after the tenant's abandonment, effects a termination of the liability of the tenant under the rent covenant.[2] It is apparent, therefore, that provability of a landlord's claim presupposes repossession by the landlord and occupation of the premises by the landlord or reletting, without regard to whether the landlord's acts had the effect of terminating the tenant's liability on the rent covenant under the applicable state law of landlord and tenant.

(3) If allowability were conditioned on failure to terminate, the claim would have to be reserved; but present allowance is expressly contemplated by the statute: In the District Court the respondent Preferred Stockholders' Protective Committee argued that the statute provides that termination of the tenant's liability on the lease at any time prior to confirmation of the plan would bar the landlord's claim. Logically, if termination of the tenant's liability on the lease at any time after rejection has any materiality, the

[1] See the petitioners' brief in *Kuehner and Fischer* v. *Murphy* (No. 354), page 12.

[2] Certainly there is nothing to indicate that Congress intended to distinguish between a landlord who, upon repossession after rejection, occupies the premises himself, and one who thereupon relets.

claim could not be allowed at all, because of the possibility of the termination of the tenant's liability at some time prior to the expiration of the term. The claim in that event would have to be reserved as a charge against the assets of the company, and the landlord would not be entitled to vote upon the plan, since only the owners of *allowed* claims are entitled to vote upon the acceptance of a plan (subdivision (e) (1), Section 77B[1]). Yet this would be in the teeth of the rejection provision, which provides that "any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its *acceptance* and confirmation, be deemed to be a creditor". This clearly evidences an intention that the landlord's claim shall be allowed before any plan is confirmed.

Thus under the Bankruptcy Act prior to its amendment, provability was denied by Congress because the state law of landlord and tenant made the claim too contingent. In enacting Section 77B and amending Section 63(a), Congress obviously intended to change the rule of the *Manhattan Properties* case, to provide that the technical law of landlord and tenant of the states should not be applied in the administration of the federal bankruptcy law, and that instead, for the purpose of administration of the bankruptcy law, leases should be placed upon the same footing as executory contracts relating to personalty. Rejection of the lease, for the purpose of administration of the act (whatever the effect may be under the applicable

[1] Subdivision (e) (1) provides:

> "A plan of reorganization shall not be confirmed until after it has been accepted * * *, and such acceptance shall have been filed in the proceeding by or on behalf of creditors holding two-thirds in amount of the claims in each class whose claims have been *allowed*. * * *"

state law in the event that the proceedings ultimately should be discontinued without a reorganization being effected), effects an anticipatory breach and termination of the lease, and termination under the state law thereafter is immaterial so far as the operation of the statute is concerned. See Keegan, Rights of Landlord and His Bankrupt Tenant, 21 A. B. A. J. 379, 383; 2 Univ. of Chic. L. Rev. 629.

(c) *Rejection Prior to Section 77B.*

The Court of Appeals itself recognized in its decisions in the *Paramount Publix* case and on the appeal of *Kuehner and Fischer, supra,* that the rejection provision is applicable to rejection prior to the enactment of the statute. See also subdivisions (a) and (p), *supra,* at page 3. The issue, thus, is simply as to the meaning of the provision, not as to its applicability to the case at bar.

The same phraseology in the same sentence of the statute covers both rejection before enactment of the statute and rejection after its enactment, without any restrictive qualification as to prior rejection:

> "*In case an* executory contract or *unexpired lease of real estate* shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or *shall have been rejected by a trustee* or receiver *in bankruptcy* or receiver in equity, *in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall,* for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor."

Therefore, Congress must have intended the statute to have the same operation and effect in both cases.

As this Court said in *Moore Ice Cream Co.* v. *Rose*, 289 U. S. 373, 378:

> "There is a unity of verbal structure that is a symptom of an inner unity, a unity of plan and function. The field of operation is not shifted between the clauses of a sentence."

As we have seen, reentry, and occupation of the premises by the landlord or reletting, after rejection in a proceeding under Section 77B, not only do not bar the claim, whether or not the effect of the landlord's acts is to terminate the tenant's liability under the applicable state law, but are actually contemplated by the statute. Similarly in the case at bar the restoration of the premises and reletting by the landlord after rejection by the trustee in bankruptcy in the prior bankruptcy proceeding do not defeat the claim, whether or not the landlord's acts effected a surrender of the lease by operation of law under the law of New Jersey.[1]

In its opinion on the appeal of *Kuehner and Fischer, supra,* the Court of Appeals said that it is not necessary to read the rejection provision as having the effect of making over the contract of the parties "by imposing a liability for future rent on the lessee after the term had ended" (at p. 37).[2]

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[1] The argument in this brief—that termination after rejection is immaterial—is intended to be restricted to the facts of the instant case, to wit, to a termination resulting from restoring and reletting the premises. The termination in the instant case did not result from an *express release* of a tenant from all obligations under the lease in return for a consideration, or from an *assignment agreement* providing for the acceptance of a surrender in return for an express consideration.

[2] But the rejection provision does not impose "a liability *for future rent* on the lessee after the term has ended". It merely recognizes a claim for *damages* after the term is ended because of the tenant's previous bankruptcy.

The Court said further:

> "It is enough if the language be taken to mean that the 'rejection' of a lease shall be a present breach of all the lessee's promises, either to pay rent, to rebuild, to cover taxes or whatever else they may be. *Indeed, if it continues his liability after reentry, it was redundant to include covenants 'for damages or indemnity'.*"

The first sentence of this quotation would seem to require a conclusion that it was the intention to make a claim based on rejection allowable, irrespective of termination thereafter. The second sentence, which appears to state the court's reason for retreating from this conclusion, is fallacious, for it assumes that the limitation provision, from which the words "for damages or indemnity" were quoted, made claims allowable. In fact, the inclusion of those words in the limitation provision following the rejection provision was simply to make clear that a claim based on a lease containing a covenant "for damages or indemnity" was to be "limited" as well as a claim "for injury resulting from the rejection".[1]

The rejection provision, as applied to a rejection prior to the statute, cannot be restricted to leases containing special covenants any more reasonably than when applied to a rejection in a proceeding under Section 77B, which, as we have seen, is not tenable (see *supra*, p. 17). In a subsequent decision, already

[1] Claims under covenants for damages or indemnity (whether or not the lease was rejected before termination) would have been provable under the broad definition of creditors already set forth in subdivision (b) (10), which includes holders of claims under executory contracts, *whether or not such claims would otherwise be provable.* But for the inclusion in the limitation provision of a claim "for damages or indemnity", as well as a claim for injury resulting from rejection, the former might not have been limited.

referred to, the Court of Appeals recognized this and expanded its conception of the meaning of the rejection provision as applied to a rejection prior to the enactment of the statute to include a claim based on a rejected lease without special covenants which had been kept alive after rejection. *In re Paramount Publix Corp.* (*Madison-Toledo Co.* v. *Paramount Pictures, Inc.*), *supra.* In that case at the date of the original bankruptcy the premises had been entirely sublet and the landlord did nothing after rejection by the trustee in bankruptcy except to collect rents from the sub-tenant then in possession. Thus, under the doctrine of the *Paramount Publix* decision, the petitioner's claim in the case at bar would have been allowable if the landlord had merely continued to collect rent from the sub-tenants in possession.[1]

Certainly, Congress did not intend the allowability of landlords' claims to be dependent upon such technicalities of state law. Indeed its object in including the rejection provision in Section 77B and in Section 63(a) was to end the necessity of dealing with the

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[1] One sentence in the opinion of the Court of Appeals in the *Paramount Publix* case evidences the inconsistency between its decision in the case at bar and its view of the effect of the rejection in the prior bankruptcy proceeding (p. 86):

> "*As the lease was not terminated under the Ohio law until it was rejected* by the debtor's trustees, the claim should have been allowed for the rent and taxes due on the date of the rejection and for injury, if proved, due to the rejection."

If the rejection in the prior bankruptcy proceeding terminated the lease *for the purpose of the application of Section 77B*, then any subsequent termination under the state law [at least any resulting from surrender by operation of law] after such rejection [and termination] ought to be utterly immaterial.

In an opinion in these proceedings on the claim of *Evelyn Picker and Myrtle Picker*, not reported (decided March 16, 1936), District Judge Coxe also refers to rejection by the trustee in bankruptcy of this debtor as having terminated the subleases previously made by the debtor.

quaintly spelled maxims of Lord Coke. Nor does the construction of the Court of Appeals conform to the familiar direction that a remedial statute, which Section 77B obviously is, should be interpreted liberally and reasonably and in accordance with the fair import of its terms. *City of Chelsea* v. *Dolan*, 24 F. (2d) 522; *Emerson* v. *Castor*, 236 Fed. 29, 33.

(d) *If the Construction of the Court of Appeals be Adopted, the Rejection Provision, as Applied to Prior Rejection, Is Rendered Practically Meaningless. Moreover, Grossly Inequitable Results Would Follow.*

(1) The narrow construction of the Court of Appeals practically nullifies the rejection provision as applied to a rejection prior to the enactment of the statute:

(a) *Number of landlords benefited:* The only landlord who, as a practical matter, might be benefited by the rejection provision under the doctrine of the Court of Appeals is the one who was fortunate enough to have had the premises entirely sublet by the tenant at the time of bankruptcy (*Paramount Publix* case). Such a landlord was in a position to reap income from his property without terminating the lease by collecting rent from the subtenants so long as they remained in possession. Where the premises were not sublet, the landlord in order to realize value from his property was compelled to reenter and occupy himself or relet. Obviously, no landlord would have allowed the premises to remain idle in the hope of collecting the full rent against an undischarged corporate bankrupt. Yet the landlord's occupation or reletting generally had

the effect of terminating the lease,[1] although both as a practical matter merely had the effect of mitigating the landlord's damages. Thus, if Congress had any intention of benefiting landlords whose leases had been rejected prior to the enactment of the statute, it must be deemed to have intended to benefit the great majority of that class of landlords and not the paltry few who were not compelled to terminate. Otherwise provability would depend upon fortuitous circumstances—such as the state in which the premises were located, or whether the premises had been sublet, or whether the premises had been occupied by the landlord instead of relet, or whether the premises had been substantially altered by the tenant before abandonment.

The natural common sense meaning of "injury resulting *from the rejection*" means the injury which the landlord suffered as a result of the release of the assets in the bankrupt estate from liability for rent under the lease. The liability of the corporate *debtor* which survived rejection, whatever may have been its value, would be terminated, in any event, by the final decree in these proceedings. Its termination before final decree, but after rejection, therefore, was naturally deemed of no significance by Congress.

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[1] In no state could the landlord occupy the premises himself without terminating the lease, and even in those states in which he ordinarily could relet without terminating the lease (see *infra*, p. 45), he could not, where the condition of the property made it impossible to relet without changing the alterations made by the tenant and restoring the premises to their original condition, for under the doctrine of the Court of Appeals such restoration itself would terminate the lease.

For instance, in the case at bar the landlord could not have relet without restoring the wall between the two buildings and she could not restore without, as the Court of Appeals held, effecting a surrender. Thus she would have had to allow the premises to remain idle from November, 1932, in order to preserve her claim.

(b) *Amount of damages*: Under the construction adopted below, the landlord must, in order to have retained his claim, have allowed the premises to remain unoccupied after rejection, and at least up to the date of institution of proceedings under Section 77B. Two or three years may have elapsed after rejection by the trustee in bankruptcy before the enactment of Section 77B and the institution of a proceeding thereunder. Yet, under the measurement of damages which the Court of Appeals itself has laid down (appeal of *Kuehner and Fischer, supra*), the landlord's claim for such two or three year period could not exceed the difference between the rent reserved and the fair rental value of the premises for such period. If the premises were relet without loss for the remainder of the term after the institution of proceedings under Section 77B, or if the lease expired at that time, *the construction adopted by the Court of Appeals would result in the allowance of a claim for less than three years' rent and less than the loss actually suffered by the landlord.* Congress intended no such unjust result.[1]

(2) The claim is "limited" with reference to termination of the lease prior to enactment of the statute: The amount of the parity portion of a landlord's claim for injury resulting from rejection is expressly measured with reference to the "date of surrender of the premises to the landlord or the date of reentry of the land-

[1] Yet the only alternative would be to apply a different measure of damages to claims based on rejection prior to the statute so that in the case of such claims the measure of damages would be the full amount of the rent reserved for the period intervening between the date of the rejection by the trustee in bankruptcy and the date of institution of proceedings under Section 77B (although the premises could have been relet for 100% of the rent originally reserved in the lease, or more). Such a rule would be unjust to other creditors.

lord, whichever first occurs, whether *before* or after the filing of the *petition*". Reentry, as we have seen, means a technical reentry terminating the tenant's liability. It could not have been intended to limit this provision to termination of liability on the lease *after* the enactment of *the statute* but *before* the filing of *the petition* thereunder, for the statute clearly contemplated that a petition might be filed immediately upon its enactment (*i. e.*, its effective date). Hence, the statute must have contemplated the landlord's termination of the tenant's liability on the lease by reentry before the enactment of the statute (but after rejection in the prior bankruptcy proceeding).[1]

(3) If restricted to a lease which has been kept alive, the rejection provision is rendered superfluous as to prior rejections: A lease which was kept alive after rejection would have remained vested in the bankrupt tenant (*In re Frazin, et al.*, 183 Fed. 28), and consequently, upon the filing of a petition under Section 77B would have fallen into the reorganization estate. In such event the debtor or the reorganization trustee would have had to reject the lease again, if burdensome. Consequently, any landlord's claim could in such event be based upon the provision which relates to rejection "pursuant to direction of the judge given in a proceeding instituted under" Section 77B, and the reference to *rejection in a prior proceeding* would be redundant.

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[1] Of course, the lease must not have terminated prior to the institution of the original bankruptcy proceeding, for in that event the trustee would have had nothing to reject. It is for this reason, no doubt, that the amendment to Section 63(a) does not, as does Section 77B, measure the amount in which the claim may be allowed with reference to surrender or reentry of the premises "*before or after the filing of the petition.*"

(4) The construction of the Court of Appeals would bar a claim under Section 77B, though provable in a prior bankruptcy proceeding: In an ordinary bankruptcy proceeding where Section 63(a), as amended, is applicable, the landlord would have a provable claim to the extent of at least one year's rent. If after his claim has been allowed the landlord should reenter and terminate the lease and the bankrupt should then file a petition under Section 77B, under the doctrine laid down by the Court of Appeals in the case at bar, the landlord would have no provable claim under Section 77B at all; for, at the date of the institution of the proceeding under Section 77B the tenant would be under no liability to the landlord under the applicable state law because of the prior termination. There is certainly nothing to indicate that Congress intended that the landlord in the latter case should lose his claim.[1]

Yet it is obvious that the language relating to rejection in a proceeding pending "prior to the institution of a proceeding under" Section 77B, cannot cover the landlord's claim in the case supposed without also covering the landlord's claim in the case at bar, since, as we have already shown, the rejection provision of the statute applies, in identical language, to rejections prior to the enactment of the statute as well as to rejections after its enactment.[2] The provision

[1] On the contrary, Congress clearly intended that, if the bankruptcy liquidation proceedings should be converted into reorganization proceedings (in which shareholders might participate), the landlord's claim should be increased, to an amount equal to three years' rent (so far as other creditors are concerned) and to the full amount of his claim (so far as stockholders are concerned).

[2] Moreover, Congress no doubt realized that the conversion of a bankruptcy liquidation proceeding into a reorganization proceeding under Section 77B would, no doubt, be very infrequent in the future, since corporations ordinarily would avail themselves of Section 77B before resorting to liquidation.

obviously was intended to have the same effect in both cases and to allow the landlord to establish a claim for the injury which was inflicted on him by the refusal of the trustee in bankruptcy to assume the lease as an obligation of the estate.

(e) *The Statute Does Not "Create" a Substantive Right.*

The only argument that has been made against the construction for which the petitioner contends is that Congress did not intend to create a legal claim[1] or substantive right where none theretofore existed at common law or in equity. But the statute, if construed as contended for, does not create a substantive right where none previously existed [either where the lease was terminated prior to the enactment of the statute, but after rejection in the prior bankruptcy proceeding; or where the lease is terminated after the statute (and after rejection in a bankruptcy or equity proceeding instituted after the enactment of the statute) but before the institution of proceedings under Section 77B]. *In both cases the leases were in existence at the time of the institution of the original bankruptcy or equity proceeding.*

Properly viewed, therefore, *the question in the case at bar is not whether Congress intended to create a right where none existed theretofore, but whether it intended that a new division of "the pot" should be made* among the creditors of a tenant whose assets

[1] The Special Master (R. 39) so phrased his argument. The statute obviously did create *claims* where none theretofore existed, for it created a claim for *damages* unknown to the common law. What the Master means is that the statute did not create any *substantive rights* against a debtor where none existed prior to the enactment of the statute.

were still being administered by the bankruptcy court at the time the purpose of the bankruptcy proceeding was converted from liquidation to reorganization pursuant to the statute, including among such creditors all those who had valid leases in existence at the time of institution of the proceeding. It is clear that Congress did intend to change the rule of the *Manhattan Properties* case and thus to provide for such a new division of the pot, both in proceedings instituted after the enactment of the Act of June 7, 1934, and also in bankruptcy proceedings pending at the date of its enactment:

> (1) where the time for filing claims had not expired,[1] or
>
> (2) where, whether or not the time for filing claims in the bankruptcy proceeding had expired,[2] a petition for reorganization under Sec-

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[1] The Act of June 18, 1934, 48 Stat. 991, further amended Section 63(a), as amended by the Act of June 7, 1934, to provide "that the provisions of this clause (7) shall apply to estates pending at the time of the enactment of this amendatory Act *in which the time for filing such claims has not expired.*" The evident purpose of this amendment was to avoid the confusion and disorganization which would have resulted if the time for filing claims had to be reopened and a redivision of the bankrupt estate made.

[2] The District Court was obviously wrong in thinking (R. 50-1) that the rejection provision in Section 77B was applicable only if the petition under Section 77B was filed prior to the expiration of the period for filing claims in the prior bankruptcy proceeding. The Act of June 18, 1934, amended only Section 63(a), not Section 77B. Subdivision (c)(6) of Section 77B expressly directs the reopening of the time for filing claims, whether or not the time for filing claims in the prior bankruptcy proceeding has expired. The district court's conception as to the relevancy of the time for filing claims in the prior bankruptcy proceeding was rejected by the Court of Appeals in its decisions in the *Paramount Publix* case, *supra*, and on the appeal of *Kuehner and Fischer* in these proceedings, *supra*.

tion 77B should be filed in such bankruptcy proceeding and approved by the court.[1]

The language and scheme of the statute seem to us so clear and unambiguous as to compel this conclusion without the necessity of examining the legislative history of the statute or the conditions which existed at the time of the enactment of the statute (*Helvering* v. *City Bank Farmers Trust Company*, 296 U. S. 85, 89). As we have seen, however, reference to the legislative history of the statute and the contemporaneous conditions existing at the time of the enactment of the statute confirm the plain meaning of the language used, and the unreasonable results which would be effected by the adoption of the narrow construction of the Court of Appeals are strongly persuasive reasons against it.

If Congress intended the statute to mean something other than what the language used plainly means, it would have retained the original proviso clause in the House bill, which would have barred the claim of any landlord who terminated his lease before the enactment of the statute or any time after the enactment of the statute up to the time of the allowance of the claim in the proceeding under Section 77B; or, at least it would have inserted a less stringent qualification, such as "provided that the lease has not or shall not have been terminated prior to the institution of proceedings under this Act". The absence of any qualification in the language used and the elimination of the qualification initially used, we submit, compels the

[1] In *In re Paramount Publix Corporation, Greenberg* v. *Paramount Pictures, Inc.*, 85 F. (2d) 42, 44, the court below said of a situation like that in the case at bar:

> "* * * reorganization becomes an amplification or new end product of the original bankruptcy, just as though the bankrupt * * * had proposed a composition. * * *"

conclusion, particularly in view of the remedial purpose of the statute, that termination by surrender or reentry before the enactment of the statute does not bar the claim under Section 77B.

The construction adopted by the Court of Appeals ignores every one of the extraordinary consequences which flow therefrom, and its decision, we submit, is equivalent to judicial legislation.

POINT II.

There are no doubts as to the constitutionality of the statute which can influence its interpretation.

(a) *The language of the statute is clear and unambiguous.*

The trustee urges that the plain language of the statute should not be followed in the case at bar because that would give it a retroactive effect which would "create" a claim where none existed before and would deprive the debtor of a vested defense which it theretofore had to any cause of action which might have been brought against it on the lease.

It has not been suggested that there is any doubt as to the constitutionality of the statute in its prospective operation,—*i. e.*, as applied to leases which were subsisting obligations at the date of enactment, irrespective of whether they were rejected before or after the enactment of the statute, and irrespective of whether or not the debtor corporation may have been relieved of all liability prior to the institution of proceedings for reorganization.

Nor, apparently, is it urged that the language of the rejection provision permits it to be given a

different meaning as applied retroactively to the petitioner's claim from the meaning which clearly must be given to it in its prospective operation. The trustee's argument appears to be merely that the statute cannot be applied to the claim in the case at bar because its retroactive operation in this case would raise doubts as to its constitutionality.

It is true that doubts as to constitutionality may influence the *interpretation* of a statute, but the Court of Appeals did not suggest any permissible interpretation of the language of the statute which would exclude the petitioner's claim. In fact, the Court did not even attempt to interpret the statute, but only refused to *apply* it to the petitioner's claim because of doubts as to its constitutionality. In so holding, the Court of Appeals has, in effect, invalidated and stricken down the statute as applied to this case, which was beyond its power, since no direct attack had been made on its constitutionality.

The only suggestion made by the Court of Appeals which can in any sense be deemed to be an interpretation of the rejection provision is its statement in its opinion on the appeal in these proceedings of *Otis Estate Land Trust,* 83 F. (2d) 202, 206, where it said:

> "But there is no new definition of a claim; only of a creditor."

Obviously, however, if a landlord is deemed to be a *creditor,* he must be deemed to have a *claim* entitled to participate in the reorganization. Otherwise the rejection provision is entirely meaningless. For, if the doctrine of the Court of Appeals (that there must be a lease in existence at the time of the enactment of the statute) is correct, the definition of creditors and claims in subdivision (b)(10) would

have been sufficient to make every landlord's claim allowable which in its view would be allowable under the rejection provision. But the rejection provision is not meaningless either in its retrospective or prospective application. By including the provision as to prior rejections, Congress obviously intended to permit landlords like the petitioner to participate in a reorganization and, while so doing, it also included language covering rejections in the future in order to make it clear beyond doubt that claims based on leases without special covenants should be allowable.

As we have shown, (1) the statute is expressly applicable to prior rejections (*supra*, p. 21); (2) Congress did not intend to exclude the landlord whose lease did not contain a special covenant for damages or indemnity (*supra*, pp. 17, 24); and (3) it eliminated from the House bill the *proviso* which had excluded the landlord whose lease had been or should be terminated after rejection and inserted in place thereof a provision which measured a part of his claim with reference to the date of his reentry, whether *before* or after the enactment of the statute (*supra*, pp. 13, 32). In short, the meaning of the statute is so clear that doubts as to its constitutionality as retroactively applied cannot influence its interpretation. Such doubts, however grave they may be, will not authorize the courts to adopt an interpretation which is patently at variance both with its express terms and with its plain intent.

As this Court said in *Moore Ice Cream Co.* v. *Rose*, *supra*, at page 379:

> "But avoidance of a difficulty will not be pressed to the point of disingenuous evasion. Here the intention of the Congress is revealed too

distinctly to permit us to ignore it because of mere misgivings as to power."

(b) *No question as to the constitutionality of the statute has been raised in the case at bar; none of the respondents was in a position to question its constitutionality.*

Neither the trustee nor any other respondent has at any time directly questioned the constitutionality of the statute if it be interpreted as permitting the allowance of the petitioner's claim. Its constitutionality cannot be attacked for the first time in this Court.

Moreover, none of the respondents was in a position to attack directly the constitutionality of the statute for certain reasons which, we submit, also make unavailable to them the argument of constitutional doubts in aid of statutory interpretation, by which they seek indirectly to inject the question of constitutionality into this case.

The trustee has no independent standing to question the constitutionality of the statute. Its right in that respect cannot rise higher than the rights of those whom it represents; (1) the debtor and its stockholders, and (2) other creditors. Neither creditors nor stockholders are in a position in this case to attack the constitutionality of the provision which the statute has made for this petitioner.

(1) *As to creditors.*

The only injury of which creditors of the debtor whose claims were allowed in the prior bankruptcy proceeding before Section 77B was enacted can complain is that the treatment of part of the claim of the petitioner and those similarly situated on a parity with their claims would dilute their participation in the

reorganization. Consequently, the only provision of the statute the constitutionality of which they or the trustee on their behalf could have attacked is the limitation provision requiring landlords' claims to be treated on a *parity* with other claims to the extent of three years' rent.

But the parity provision is clearly severable. Even if it had been directly attacked and invalidated, that would not have stricken down the rejection provision on which depends the general allowability of the petitioner's claim. Therefore, even if doubts as to the constitutionality of the parity provision could affect *its* interpretation, they cannot affect the interpretation of the *rejection* provision.

However, it cannot be urged that the parity provision should be construed so as to deny landlords' claims partial parity with other creditors, for its language is indisputably plain and unambiguous in this respect and can have no meaning other than that claims which are made allowable by the rejection provision (claims "for injury resulting from the rejection") shall be treated on a parity with other claims to a limited extent.

In any event, there is no serious doubt as to the power of Congress to accord to the petitioner's claim a ranking on a parity with claims already established in the bankruptcy proceeding. While under the state law creditors had a right to enforcement of their respective claims in priority to the interests of stockholders, they obviously had no right under that law, nor under the terms of their contracts, to enforcement of their claims in priority to landlords, to whom their debtor was also legally obligated. Nor may the provisions of the Bankruptcy Act as they existed at the time of the extension of credit be read into the contracts of the creditors, for Congress "may amend or repeal [the Bankruptcy Act] at

pleasure, provided it does not disregard the requirement of uniformity." *City of Chelsea* v. *Dolan,* 24 F. (2d) 522, 523. Creditors had no vested interest in the then provisions of the Bankruptcy Act, even after the filing of their debtor's petition in bankruptcy. Congress could change the then existing bankruptcy system, even after the filing of the petition. *City of Chelsea* v. *Dolan, supra.*

(2) *As to the debtor and its stockholders.*

The statute does not have the effect of destroying the vested defense which the debtor would have under the applicable state law in the event that the reorganization proceedings should be dismissed. The statute merely changed the statutory rule of non-provability and provided that termination of the lease should not deprive those who had valid leases at the time of the original bankruptcy from participating in the debtor's reorganization. Neither the debtor nor its stockholders may complain of that.

The debtor corporation voluntarily filed its petition for reorganization under Section 77B. The debtor cannot avail itself of the benefits of the statute and at the same time seek to escape its burdens. *Great Falls Mfg. Co.* v. *Attorney General,* 124 U. S. 581; *Wall* v. *Parrot Silver & Copper Co.,* 244 U. S. 407; *St. Louis Casting Co.* v. *Prendergast Const. Co.,* 260 U. S. 469. The stockholders of the debtor by acquiescing in the debtor's seeking relief under Section 77B have similarly estopped themselves.

Congress might have restricted the benefits of the statute to going corporations not already in bankruptcy. It was a matter of grace to extend its benefits to corporations which already had been adjudicated bankrupt. It was reasonable for Congress to provide that, if a corporation which had already been adjudi-

cated bankrupt desired to effect a reorganization under the provisions of the new statute, all persons to whom it was legally obligated at the time it originally went into bankruptcy should be permitted to participate in such reorganization, and particularly all persons who suffered injury as the result of the bankruptcy.

Whether or not these considerations are equally applicable to the case of a debtor which has involuntarily been subjected to the provisions of Section 77B, it is clear that doubt as to the constitutionality of the rejection provision in a case where an involuntary petition has been filed under Section 77B cannot affect its construction in the case of a voluntary petition as in the case at bar. Even if unconstitutional in an involuntary case, there is nothing to indicate that Congress did not intend that the provision should be applicable in a voluntary case. If in a case involving an involuntary proceeding, the provision should be held unconstitutional (as applied to leases terminated before the enactment of the statute) there would result merely a functional severance of the rejection provision and its restriction to voluntary proceedings. *Cf. Loeb* v. *Columbia Township Trustees,* 179 U. S. 472, 490; *People* v. *Knapp,* 230 N. Y. 48, 60.

(c) *Even if the debtor or its stockholders could have attacked the constitutionality of the statute, general principles of constitutional law would support its validity.*

The power of Congress over the "subject of bankruptcies" extends to whatever is necessary or *reasonably adapted* "under modern conditions to deal adequately with the relationship existing between embarrassed debtors and their creditors". *Campbell* v. *Al-*

leghany Corp., 75 F. (2d) 947, 955, cer. den. 296 U. S. 581; *In re Reiman*, 20 Fed. Cas. 490, 496; see also, *Hanover National Bank* v. *Moyses*, 186 U. S. 181; *In the Matter of Edward Klein*, 42 U. S. 277; *Continental Bank* v. *Rock Island Ry.*, 294 U. S. 648, 670; *Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S. 555, 582, *et seq.*

It is within the bankruptcy power to provide for the provability or nonprovability of claims. *Manhattan Properties, Inc.* v. *Irving Trust Co., supra.*[1] Provision for provability is merely incidental to an equitable distribution of a debtor's property among his creditors *as of the date of the institution of the bankruptcy proceeding*, which is one of the ends of a bankruptcy law. *Kothe* v. *R. C. Taylor Trust, supra*, at page 227, and cases cited in *Louisville Bank* v. *Radford, supra*, at page 507.

Even if after the petition was filed in the case at bar and before the claim was made provable, the debtor's *individual liability* on the lease had been terminated under the applicable state law, that would not have insulated the *bankrupt estate* from the exercise by Congress of its power to provide for the provability of the claims of all persons to whom the bankrupt was legally obligated at the time of bankruptcy.

The plenary power of Congress to legislate on the subject of bankruptcies is sufficient to widen the class of persons entitled to participate in the reorganization of an estate already in bankruptcy, even if the provision for participation disregards *vested defenses*

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[1] This Court said (at p. 332), "The issue is not one of power, for plainly Congress may permit such claims or exclude them."

accrued prior to its enactment. *Cf. Norman* v. *B. & O. R. Co.*, 294 U. S. 240, and cases cited therein.[1] The bonds involved in *United States* v. *Bankers Trust Co.* (reported *sub nom. Norman* v. *B. & O. R. Co.*, 294 U. S. at p. 294) had become payable prior to the enactment of the resolution striking down "gold clauses", and the cause of action thereon had vested. There is obviously no difference between a *vested cause of action* arising out of a contract, such as there involved, and a *vested defense* arising out of the local law, such as involved in the case at bar.

The only limitation is that the provision enacted pursuant to the federal power shall bear a reasonable relation to an end connected with the object of the power. The provision for provability in Section 77B is not arbitrary, but does, as we have seen, bear a reasonable relation to a legitimate end,—viz., to achieve an equitable participation in the debtor's assets by those to whom the debtor was obligated as of the date of the original bankruptcy, where reorganization was sought by a corporation already in bankruptcy or by its creditors or stockholders.

Possibly Congress might constitutionally have excluded landlords whose leases had been terminated under the applicable state law. But it certainly is true that letting in those landlords is not only not arbitrary and unfair, but is the only equitable provision that Congress could have made, in recognition of the fact that their injury, which resulted from the bankruptcy proceeding, had been as real as the

[1] None of the cases cited by the trustee in its brief in opposition to the granting of a writ (p. 15) holding that a vested defense cannot be destroyed by subsequent legislative action involves a statute enacted under a federal power.

injury inflicted on other landlords whose leases had not been terminated.

In the case at bar the lease was a valid subsisting obligation of the debtor at the date it filed its voluntary petition in bankruptcy in 1932. In no proper sense, therefore, does the statute *create* a substantive right. The debtor and its stockholders, after filing the original voluntary petition in bankruptcy in 1932, had no interest in the assets of the debtor entitled to constitutional protection other than the right to any surplus of assets which might result after the payment in full of its creditors as of the time it originally availed itself of the bankruptcy process. The provision in question is not in the least analogous to a subsequently enacted provision (to which the trustee referred in its brief (p. 14) in opposition to the granting of a writ) providing that claims which are not valid at the time of the filing of the petition (such as those subject to the defenses of the statute of limitation, the statute of frauds, or the statute of usury) shall nevertheless be provable. Obviously the rejection provision applies only to *valid leases* subject to no defenses at the time of rejection by the trustee in the prior bankruptcy proceeding.

Section 77B, however, goes no further than to do away for the purpose of the bankruptcy law with the historical distinction between leases and other types of obligations, all of which were valid at the time of the institution of the original bankruptcy proceedings, and to provide, as a condition of the acceptance of the benefits of the reorganization statute in bankruptcy proceedings pending at the date of its enactment, that the rights and priorities of the creditors and stockholders should be adjusted

in accordance with their substantive rights as they existed at the time of the original bankruptcy.[1]

POINT III.

Under the law of New Jersey the liability of the debtor under the lease survived restoration and reletting of the premises.

Even under the doctrine of the Court of Appeals, as enunciated in the *Paramount Publix* case (*supra*, p. 24), the petitioner's claim is allowable if at the time of the institution of proceedings under Section 77B the debtor was still liable on the lease under the law of New Jersey, the situs of the property.

The burden of proving facts establishing a surrender rests on the party alleging surrender. *O'Neil* v. *Pearse*, 87 N. J. L. 382, aff'd. 88 N. J. L. 733; *Liskovsky* v. *Blau*, 114 N. J. L. 324; *Shalet* v. *Klauder*, 34 F. (2d) 594. The only facts bearing on the question whether a surrender was effected which were established by the trustee (by including them in the two stipulations of fact which constitute the only evidence in the case [R. 19, 33]) are these:

The debtor upon its adjudication on August 28, 1932, abandoned the premises. The trustee in bankruptcy thereafter collected rents from the sub-tenants in possession, but on November 11, 1932, rejected the

[1] The claim made provable is for *damages* only, so that subsequent termination of the lease would have been contemplated if the statute had been enacted prior to the commencement of the original bankruptcy proceedings in 1932 (see *supra*, p. 18). The final decree will release the debtor and its assets from all liability for future rent, as would the state law if the proceedings were dismissed.

lease and abandoned the premises. After rejection of the lease, the landlord relet various portions of the premises to sub-tenants in possession and subsequently relet other portions of the premises to others. The lease contained no clause expressly authorizing the landlord upon the tenant's abandonment or default to relet for the tenant's account; nor, on the other hand, did it provide that the term of the lease should end upon the landlord's re-entry or re-possession after the tenant's abandonment or bankruptcy (R. 23).

The stipulations were silent as to whether the landlord in reletting intended to relet for the debtor's account or to accept a surrender.

As has been mentioned (*supra*, p. 3), though the stipulations were silent on the subject, the Master "found" that the landlord had filed in the bankruptcy proceeding "a claim for $1,980.99 for alleged expenditures in restoring a party wall and in closing up a common entrance in the demised premises". The Court of Appeals went further and "found" (R. 72) that the debtor before reletting "made structural changes in the premises to restore them to the condition they were in when leased by rebuilding a party wall and closing up a common entrance, all at an expense of $1,980.99." Although not established by the record and not drawn in issue by the trustee's objection to the claim (and although for that reason alone the affirmance of the Court of Appeals on the ground that the landlord restored the premises as mentioned is reversible error, as we show in Point IV), it will be assumed *arguendo* for the purpose of this point that the record does establish that the landlord restored the premises in the manner stated in the opinion of the Court of Appeals and that the legal effect of the restoration is in issue.

(a) *Reletting After the Tenant's Abandonment of the Premises Does Not Effect a Surrender Under the Law of New Jersey.*

Although at common law and in New York and some other states reletting after the tenant's abandonment of the premises effects an acceptance of a surrender unless the tenant *agrees* to a reletting for the tenant's account (*Gray* v. *Kaufman Dairy & Ice Cream Co.*, 162 N. Y. 388),[1] the general rule in this country is to the effect that in such event the landlord may relet without accepting a surrender and may recover the difference between the rent reserved in the lease and the rent received on reletting, even though the lease contains no provision expressly authorizing the landlord to relet as the tenant's agent. 16 R. C. L. Sec. 672; 13 L. R. A. (N. S.) 398; 3 A. L. R. 1080; Tiffany, Landlord and Tenant (1910) page 1338; Tiffany, Real Property (1920) page 1586. In most jurisdictions following this general rule it is held that the landlord's reletting releases the tenant from further liability unless the landlord notifies the tenant before reletting that he intends to relet for the latter's account. However, in New Jersey (which also follows the general rule), the giving of such notice by the landlord is not a prerequisite to the survival of the tenant's liability,[2] but the party asserting

[1] Under the common law doctrine mere notice by the landlord of intention to relet for the account of the tenant is ineffectual.

[2] The same rule is followed in a number of other states: *Martin* v. *Siegley*, 123 Wash. 683; *Auer* v. *Hoffman*, 132 Wis. 620; *Miller* v. *Benton*, 55 Conn. 529; *Marshall* v. *John Grosse Clothing Co.*, 184 Ill. 421; *J. C. Meyer & Co.* v. *Smith*, 33 Ark. 627; *Scott* v. *Beecher*, 91 Mich. 590; *Sessinghaus* v. *Knocke*, 127 Mo. App. 300; *Guy* v. *Gould*, 126 Kan. 25; *Ralph* v. *Deiley*, 293 Pa. 90; *Bumiller* v. *Walker*, 95 Oh. St. 344 (see *In re Paramount Publix Corp.*, *supra*, at p. 85).

a surrender must, in order to establish it, prove acts of the parties (*other than reletting without notice*) which are inconsistent with the continued existence of the lease. *Liskovsky* v. *Blau, supra; Banks* v. *Berliner,* 95 N. J. L. 267; *Albrecht* v. *Thieme,* 97 N. J. L. 103, aff'd. 98 N. J. L. 249; *Dolton* v. *Sickel,* 66 N. J. L. 492, aff'd. 68 N. J. L. 731.[1] While mere abandonment, whether or not followed by reletting, terminates the *privity of estate* between landlord and tenant in New Jersey (*Whitcomb* v. *Brant,* 90 N. J. L. 245), it does not destroy the *privity of contract* (as does the acceptance of a surrender) and thus does not release the tenant from liability to pay rent.

The Court of Appeals itself recognized that under the New Jersey law reletting without notice did not effect a surrender, saying (R. 73):

> "Apparently proof that a lease was rejected by a receiver in bankruptcy of the lessee, that the lessor re-entered and relet without notice to the lessee of acceptance of surrender or of an intention to relet for the lessee's account, is not sufficient as a matter of law to show a surrender and acceptance of the leased premises. *Liskovsky* v. *Blau,* 114 N. J. Law, 324, 176 A. 562. See, also, *Dolton* v. *Sickel,* 66 N. J. Law, 492, 49 A. 679; *Banks* v. *Berliner,* 95 N. J. Law, 267, 113 A. 321."

Under these circumstances it would seem unnecessary to discuss this phase of the case further. A detailed analysis of the New Jersey decisions, however, may be found in Appendix A.

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[1] Thus, whereas in New York a surrender results in the absence of proof of an agreement to the contrary, in New Jersey a surrender never results unless an agreement to effect a surrender is shown. See also *Mecker* v. *Spalsbury,* 66 N. J. L. 60; *Miller* v. *Dennis,* 68 N. J. L. 320; *O'Neil* v. *Pearse, supra.*

(b) *Restoration of the Premises, Whether or Not Followed by Reletting, Does Not Effect a Surrender Under the New Jersey Law.*

After concluding that reletting without notice after the tenant's abandonment did *not* effect a surrender under the New Jersey law, the Court of Appeals concluded that the landlord's restoration of the premises did, saying (R. 73):

> "But here the evidence went beyond that [re-entry and reletting] and showed that the landlord had made substantial changes in the premises indicative of the resumption of dominion over them inconsistent with the continuing status of landlord and tenant under the lease. These acts together show such an unequivocal breaking off of the relationship which before existed under the lease that the landlord must be held to have accepted a surrender of the premises as a matter of law in consequence of what was done. *Sypherd* v. *Myers*, 80 N. J. Law, 321, 79 A. 340; *Fink* v. *Browe Co.* (N. J. Ch.), 99 A. 926."

The "substantial changes" referred to by the court are those described in an earlier part of its opinion where it is said (R. 72) that the landlord "made structural changes in the premises *to restore them to the condition they were in when leased* by rebuilding a party wall and closing up a common entrance".

The cases cited by the Court of Appeals do not support its conclusion. In the *Sypherd* case it did not appear that any repairs or alterations whatever had been made by the landlord after resuming possession. In the *Fink* case it was held merely that "making changes and alterations therein that were not necessary as repairs for the preservation of the building",

among other acts on the part of the landlord,[1] indicated an intention on the landlord's part to accept a surrender.

The citation of the *Fink* case by the Court of Appeals apparently evidences its belief that the repairs made by the landlord upon resuming possession were not necessary for the preservation of the building. But no such conclusion fairly can be drawn from the skeleton facts found by the Court of Appeals—to wit, that a party wall was rebuilt and a common entrance closed up. In the absence of anything in the record on the subject, the only inference that reasonably can be drawn as to the nature of the repairs is that the landlord upon the debtor's abandonment was compelled to restore the party wall (which the debtor had removed so that it could occupy the premises involved herein and the adjoining premises as one unit) and to close up the common entrance (which the debtor had made) in order to prevent such injury as might result from the separate occupation of the *adjoining* premises either by the debtor or by a new tenant.[2]

The New Jersey decisions clearly hold that repairs made by a landlord upon the tenant's abandonment for the purpose of preserving the premises from injury do not effect a surrender of the lease, even if accompanied by reletting. *Mecker* v. *Spalsbury*,

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[1] The landlord in the *Fink* case also accepted the keys without objection. In the case at bar the keys were not offered to nor accepted by the landlord.

[2] The tenant's alterations had seriously damaged the building. *Cf. Kinney Realty Co.* v. *Salmon*, 106 N. J. Eq. 389; *Agate* v. *Lowenbein*, 57 N. Y. 604; *Woolworth Co.* v. *Nelson*, 204 Ala. 172. The landlord merely repaired the damage.

supra;[1] *Liskovsky* v. *Blau, supra; Banks* v. *Berliner, supra; Block* v. *Bell Furniture Co.*, 111 N. J. Eq. 551, 559. The conclusion of the Court of Appeals is, therefore, erroneous in the first place, we submit, on the ground that the repairs made by the landlord were necessary to preserve the building from injury and, therefore, within the doctrine of the foregoing cases.

Assuming, *arguendo,* however, that the repairs made by the landlord in the case at bar were not necessary to preserve the premises under the doctrine of these cases (though this assumption exceeds the realm of reasonableness), it is clear that where the repairs made by the landlord go no further than to restore the premises to their original condition, even though they are not required *to preserve* the premises, such repairs do not effect a surrender, even when accompanied by reletting. *Zabriskie* v. *Sullivan,* 80 N. J. L. 673, aff'd. 82 N. J. L. 545. The Supreme Court said in the *Zabriskie* case (at p. 676):

> "The reparation of the premises by the landlord was also for the benefit of the tenant, for it relieved him of his duty to repair and increased the likelihood of securing a tenant."[2]

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[1] In the *Meeker* case, where a surrender was found, the landlord remodelled the building, which had been leased as a hotel, so that it could be used either as a hotel or for flats. The entire character of the building was thus changed; and, moreover, when the work was begun the premises were already in good condition and repair.

The facts in the *Fink* case do not show what the nature of the repairs were, the opinion merely stating the conclusion of the court that they were not necessary for the preservation of the building.

[2] The lease contained no covenant to repair, but a covenant by the tenant to surrender the premises in good condition at the expiration of the term. Hence, the repairs made were those required to restore the premises to substantially as good a condition as existed at the commencement of the term. The lease in the instant case contains both covenants (R. 27).

The general rule where reletting alone does not effect a surrender, is clearly stated by one writer (Schnebly, Operative Facts in Surrenders, 22 Ill. L. Rev. 117, 129) as follows:

> "Another question which arises is whether or not a surrender results from the fact that the lessor has made repairs before reletting. The making of necessary repairs ought not to be regarded as indicating any particular intention. It is well known that repairs must usually be made when there is a change of tenants; that new tenants will usually demand more than tenants who are settled on the premises. The old lessee is benefited by the making of such repairs if the result is to secure a new tenant more quickly, or to obtain a higher rental than would otherwise be realized. Such repairs do not, therefore, cause a surrender. Where expensive and unnecessary repairs have been made, the question is more serious. Such action on the part of the landlord may make it appear that he has taken advantage of the tenant's default to eliminate him entirely, and to make the premises a source of greater profit to himself. Moreover, the making of extensive alterations means that the premises must stand idle while these alterations are being effected, and that the loss to the tenant may be aggravated."

In the instant case the repairs were neither unnecessary nor extensive enough to prevent reletting for any appreciable period and thus aggravate the tenant's loss. On the contrary, by making the premises rentable, the debtor's damages were mitigated.

Any rule that a landlord could not restore premises to their original condition before reletting would nul-

lify the New Jersey rule that a landlord may relet for the tenant's account, since the privilege is worthless unless the landlord may put the premises in rentable condition. It is apparent that the premises in the case at bar could not have been relet as an independent unit *without four walls* and their own private entrance, and that, therefore, the landlord's repairs were necessary in order to enable her to relet.

The trustee in its brief in opposition to the application for certiorari (at pp. 16, 18) states that it is provided in the lease that "it is only upon termination of the lease that she may restore the alterations made by the debtor". The only reference to the record in support of this assertion is to the covenant in the lease relating to *improvements* (R. 28).[1] This provision merely provided that the lessor might make "such alterations and/or improvements" as it should desire, and that "said *improvements*" (not alterations) should become the property of the lessor "at the expiration or other determination of this lease". Obviously a *removed wall* and *a hole in another wall* were not *improvements* which could become the property of the landlord at any time; and it will be noted that the covenant does not state that the "alterations" made by the lessee shall ever become the property of the lessor.[2]

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[1] The provision reads as follows:

> "And the said lessee further covenants and agrees that it will, at its own expense, make such alterations and/or improvements upon the premises hereby demised as it shall desire, and lessor hereby consents to the making of any such alterations and/or improvements by lessee, *said improvements* to belong to and become the property of the lessor at the expiration or other determination of this lease."

[2] Even if the alterations made by the debtor were "improvements" within the meaning of the provision, the provision would be clearly inapplicable where the debtor abandoned the premises and the so-called improvements, as the debtor and the trustee

Thus, both principle and common sense are opposed to the conclusion of the Court of Appeals that restoration and reletting relieved the tenant from liability on the lease and, we submit, its judgment should be reversed for that reason alone, with instructions to allow the claim, subject to proof of the amount of damages.

POINT IV.

The Court of Appeals committed reversible error in affirming on the ground that the landlord restored the premises, for in so doing it decided an issue not raised either by the pleadings or the proof.

As has been stated, the trustee's objection to the claim (R. 14) raised simply one narrow issue of local law,—to wit, whether the landlord's reentering and reletting terminated the debtor's liability under the lease. It contained no allegation that the landlord had restored the premises to their former condition before reletting, nor that the restoration had the effect under the New Jersey law of effecting a surrender. The stipulations of fact, which were drawn in the light of the sole issue raised by the trustee's objection, did not stipulate that the landlord had so restored the premises nor that she had filed a claim for the expense of restoration.

Even if it be assumed that the Special Master had the right to take judicial notice of the fact that the

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did in the case at bar. The abandonment would constitute a waiver by the debtor of its rights under the clause in question. In any event, it would not follow that the restoration of the premises would effect a termination of the lease. The only result would be the liability of the debtor for the conversion of the improvements. Under the New Jersey law, it must be remembered, the landlord was clearly authorized to relet for the account of the tenant upon his abandonment.

landlord had filed a claim in the prior bankruptcy proceeding for the expense of restoration, although he was not requested to do so by any party at any time (R. 17, 18),[1] the "finding" of the Master was simply that the landlord had *filed* such a claim. His conclusion from this finding was that the filing of such a claim indicated that the landlord thought the lease had been terminated by her previous reentry and reletting because the debtor was [as the landlord alleged in her proof of claim] under no obligation to restore until the *expiration* of the term (R. 41).[2] He did not consider the restoration itself as a factor bearing on the question of whether a surrender had been effected. His report was limited to the question raised by the objection to the proof of claim and the stipulated

[1] The Special Master's report (R. 41) mentions that the "Trustee may well point to" the filing of the claim for restoration in support of its position. Actually, however, the trustee did not refer, at the hearing or in the brief submitted to the Master, to the filing of such a claim nor to the restoration. The Master, *so far as the report shows*, did not purport to take judicial notice of the filing of the claim, but referred to it, apparently, because of the personal knowledge he had acquired in acting as referee in bankruptcy in the prior bankruptcy.

The report also states (fol. 123) that "the stipulation herein shows that this claim [for restoration] is also asserted in this Reorganization proceeding", but the Master was mistaken as to this, as the two stipulations of fact (R. 19, 33) contain no reference to the filing of a claim for restoration, either in the bankruptcy proceeding or in the reorganization proceeding.

[2] This conclusion, which was not approved by the Court of Appeals, was erroneous, since the claim was provable, if at all, only on the theory that the bankruptcy petition constituted an anticipatory breach of the agreement to restore, not that the lease had actually *expired* or been terminated at a later date. *In re Metropolitan Chain Stores*, 66 F. (2d) 485, 487; *Possart* v. *Irving Trust Co.*, 69 F. (2d) 807. That this was the theory on which the proof of claim was filed is shown by the allegation in the proof of claim that "the lease has now expired *by reason of the bankruptcy*". [If it is proper to take judicial notice of the proof of claim, the allegations therein are clearly probative of the theory on which the claim was based.]

facts. The opinion of the District Court was similarly limited (R. 49).

The Court of Appeals, however, seized on the Master's finding that a claim for reimbursement of the expense of restoration had been filed and drew from it inferences of further facts,—to wit, that the repairs made by the landlord upon resuming possession were "structural changes" (R. 72) and, by implication, were not necessary for the preservation of the premises or in order to relet.

The Court of Appeals departed from the usual course of judicial procedure in "finding" that the landlord had actually restored the premises and in making certain inferences of fact in regard to the exact nature of the repairs made by the landlord. Even if the proof of claim for the expense of restoration should be deemed to be a part of the record on the issue raised by the proof of claim now before the Court, as though introduced into evidence by the trustee at the hearing before the Master, the proof of claim obviously would not be probative of the truth of the facts alleged therein,[1] any more than facts can be proved against a plaintiff by introducing a copy of his complaint in *another cause of action.*

Moreover, if the trustee's objection had raised the issue that the landlord's action in making certain repairs had effected a surrender and had introduced proof in substantiation of that objection, the petitioner could have proved the details with respect to the exact nature of the repairs made by the landlord and with respect to whether they were necessary to preserve the premises from injury after the debt-

[1] Therefore, the petitioner would have been entitled to controvert any fact stated in that proof of claim.

or's abandonment or to make them rentable. If the record had definitely shown that they were necessary to preserve the premises or to make them rentable, the Court of Appeals must have held, as we have seen from the authorities cited in Point III, that no surrender had been effected.[1] All these considerations were ignored by the Court of Appeals when it decided this question without pleadings and without evidence and without the question having been passed upon by the Special Master or the District Court.[2]

In thus proceeding the Court of Appeals has ignored the elementary principle that appellate courts should limit their decisions to issues properly framed and passed upon by the courts below, and to evidence regularly produced. *Liberty National Bank* v. *Bear*, 265 U. S. 365; *General Utilities & Operating Co.* v. *Helvering*, 296 U. S. 200; *Helvering* v. *Salvage*, 297 U. S. 106; *Compania General* v. *Collector*, 279 U. S. 306.

The *Liberty National Bank* case, *supra*, is precisely in point. This Court there held that where neither the trustee's objection to a claim nor the proof introduced by it raised an issue of law, the Court of Appeals could not base its affirmance of an order disallowing the claim on such issue, but should

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[1] As it was, the Court of Appeals ignored the fact that the Master *did not* find, although as referee in the prior bankruptcy proceeding he must have known the facts regarding the restoration, that the repairs made by the landlord were of such a nature as to change the character of the premises and thus effect a surrender by operation of law (*cf. Meeker* v. *Spalsbury*, *supra*).

[2] The trustee in its brief in opposition to the application for certiorari asserted (pp. 16, 17) that the Master found "that the alterations made by the Debtor had in fact been restored by the landlord" and that the petitioner did not except to "that finding". Since no such finding was made (R. 41), the petitioner could not except thereto. The exception was fully as broad as the "finding" made by the Master (R. 44, par. 5).

have reversed. The trustee had objected to the claim on the ground that the judgment securing it had been recovered within four months prior to bankruptcy, but it had not alleged, nor had it proved, that the bankrupt was insolvent at that time. Similarly, in the case at bar, the trustee neither alleged nor proved the landlord had made any repairs, nor did it allege that the making of such repairs had effected a surrender.

As this Court said in the *General Utilities* case, *supra* (p. 206):

> "Stipulations concerning facts and any other evidence properly are accommodated to issues adequately raised."

This Court in that case held that the Court of Appeals should not have decided the case upon a ground not presented to nor ruled upon by the Board of Tax Appeals, particularly when it had, in support of its decision, made certain inferences of fact in conflict with the stipulated facts.

It is thus clear that the Court of Appeals committed reversible error in *affirming* the judgment below. The only question that remains, therefore, is whether the judgment should be reversed with instructions to allow the claim, subject to proof as to the amount of damages, or reversed with instructions for a new trial.

The Court ought not to grant a new trial in the case at bar in view of the submission of the case on an agreed statement of facts drawn in the light of the trustee's objection.[1] Even in an action at law,

[1] Stipulations are designed to restrict issues or settle disputed facts, or both, and are binding unless cause is shown for setting them aside. *Brooklyn Mining Co.* v. *Miller*, 227 U. S. 194, 201; *United States* v. *Davison*, 1 F. (2d) 465, 469, 470; *Schmertz Wire Glass Co.* v. *Continuous Glass Press Co.*, 216 Fed. 828; *McNeill* v. *Town of Andes*, 40 Fed. 45.

where the Seventh Amendment is applicable, an appellate court will, upon a reversal of a case submitted upon an agreed statement of facts, direct the entry of final judgment without remanding for a new trial. *Thomas* v. *Matthiessen,* 232 U. S. 221, 236; *United States* v. *Illinois Surety Co.,* 226 Fed. 653, 664 (C. C. A. 7); *Massachusetts Bonding & Ins. Co.* v. *Santee,* 62 F. (2d) 724, 728 (C. C. A. 9); *Maryland Casualty Co.* v. *Beebe,* 54 F. (2d) 743, 746. The Court should, therefore, we submit, reverse with instructions to allow the claim, subject to proof as to the amount of damages.

In any event, if every other contention of the petitioner be denied, the Court should direct a new trial. In such an event, if the stipulations are not binding, or are binding only to the extent of the facts covered, both parties can introduce additional evidence as to the nature of the repairs and the necessity therefor, provided the district court permits at this late date the trustee to amend its objection to the claim.

Other relevant facts might be established on a new trial. Though the record in the case at bar shows by negative implication that the petitioner did not execute an assignment agreement such as those involved in *Otis* v. *Irving Trust Co.* (No. 436), it does not show that one was *offered* to the petitioner. However, the opinion of the Court of Appeals in the *Otis* case states (83 F. (2d) 202, 203-4) that the trustee made it a practice to offer to landlords whose leases were burdensome an agreement providing for an express surrender, in return for the execution of a release of all claims against the trustee, the bankrupt estate and the debtor (see also Record in No. 436, pp. 43-65). On a new trial the petitioner will be permitted to prove whether or not such an agreement was offered

to the landlord in the case at bar and declined. The fact that the landlord was offered and declined such an agreement, if proven, would conclusively show that she neither intended nor desired to accept a surrender or otherwise terminate the debtor's liability under the lease.

Conclusion

The judgment of the Court of Appeals should be reversed, with instructions to allow the petitioner's claim in the amount of such loss as the petitioner may prove to have been incurred, subject to the limitation provision as construed by this Court in *Kuehner and Fischer* v. *Murphy, et al.* (No. 354).

Respectfully submitted,

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Appendix A.

THE NEW JERSEY DECISIONS ESTABLISH THAT A LANDLORD MAY RELET FOR A TENANT'S ACCOUNT WITHOUT NOTICE.

In *Liskovsky* v. *Blau,* 114 N. J. L. 324, the highest court of New Jersey held that mere reletting by a landlord after the tenant's abandonment of the premises, in the absence of other evidence, is, as a matter of law, a reletting for the tenant's account, and that it does not effect a surrender.[1] So far as the facts set forth in the opinion in that case show, the lease contained no special covenant, and the landlord gave no notice to the tenant that he intended to relet for the tenant's account.

The contention made by the trustee in the Court of Appeals, which was rejected by that court, that the fact that the *record on appeal* in the *Liskovsky* case showed that the lease contained a clause expressly permitting the landlord to relet as agent for the tenant indicated that the court's decision was restricted to leases containing such special clauses, is not tenable. The court did not mention the special clause among the facts stated in its opinion. It is clear, therefore, that it chose to lay down a broad rule, rather than to base its decision on the narrow ground that the lease before it contained such a clause.[2]

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[1] The appellate court affirmed an order of the trial court directing a verdict in favor of the landlord, it appearing that the landlord had relet in his own name after the tenant and its receiver in bankruptcy had abandoned the premises.

[2] Moreover, it is well known that decisions and principles of law are applicable only to the facts stated in the opinion. *Utah Consolidated Lighting Co.* v. *Apex Mining Co.*, 285 Fed. 249, 256, cer. den. 261 U. S. 617; *Moriarty* v. *City of New York*, 132 App. Div. 10, 12, aff'd 197 N. Y. 544; *Yoders* v. *Township of Amwell,* 172 Pa. St. 447, 450; 7 R. C. L. 1003.

The broader ground of decision announced by the New Jersey

The broad rule laid down merely followed prior New Jersey decisions. *Banks* v. *Berliner*, 95 N. J. L. 267; *Albrecht* v. *Thieme*, 97 N. J. L. 103, aff'd. 98 N. J. L. 249.

In *Banks* v. *Berliner* the landlord upon the tenant's abandonment notified him that she would hold him liable for the rent, which evidenced that she did not, *by reentering*, intend to accept a surrender, but she did not notify him that she intended *to relet* for his account. Sometime thereafter it appeared that the landlord tried to relet the premises to others, and the tenant contended that the landlord's efforts had effected a surrender. It was held that the efforts to relet did not effect a surrender, and the court stated that "if she had succeeded in reletting the property, the tenant would have been entitled to have credited on his obligation the amount received under the new lease", citing *Whitcomb* v. *Brant*, 90 N. J. L. 245. Not only did the court not indicate that before making a new lease the landlord would have been required to notify the tenant that she was reletting for his account, but the citation of *Whitcomb* v. *Brant* clearly indicates that the court was of the opinion that the tenant's continued liability was not conditioned on such notice, for the opinion in the *Whitcomb* case clearly indicates that, if the landlord had been suing the tenant (instead of the tenant suing the landlord for the increased rental resulting from reletting), the tenant would have continued liable for the difference

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court may not be considered a dictum, since it appears to have been the actual ground of the decision. But even if it were a dictum to the extent that it applies to leases containing no special clauses, the dictum under the New Jersey law must be accepted as announcing the New Jersey rule in the absence of any decisions to the contrary. *Kutschinski* v. *Thompson*, 101 N. J. Eq. 649, 660.

between rent reserved and the avails of reletting, although the landlord had not notified the tenant that she was reletting for his account.[1]

In *Albrecht* v. *Thieme*, 97 N. J. L. 103, aff'd. 98 N. J. L. 249, the landlord upon the tenant's abandonment also indicated that he did not intend to accept a surrender, by advising the tenant that he would hold him accountable for any loss which he might sustain, but when he subsequently relet the premises he did not notify the tenant that he was reletting for the tenant's account. The court did not even consider whether the subsequent reletting without notice had effected a surrender, but proceeded to consider whether the reletting constituted an *eviction* of the tenant. The court concluded that there was no actual eviction because the tenant had abandoned and said (at p. 105):

> "Where, however, the tenant has vacated and abandoned the premises, an eviction by a re-letting is constructive merely and should, within the reason of the rule, impose upon the landlord no penalty other than that of crediting the tenant with the sum so earned by the property during the term."

To the same effect is *Dolton* v. *Sickel*, 66 N. J. L. 492, aff'd. 68 N. J. L. 731.

The leases involved in the *Berliner*, *Albrecht*, and *Dolton* cases did not contain any special covenant authorizing reletting for the tenant's account. Thus, under the New Jersey authorities there is no substantial difference, as far as the point now under discussion is concerned, between a lease which contains a

[1] Although the lease in the *Whitcomb* case contained a covenant expressly authorizing the landlord to relet upon the tenant's abandonment, the court did not base its dictum on this factor.

clause expressly authorizing reletting by the landlord as agent for the tenant, or which provides that the landlord may relet and apply the avails to the rent due under the first lease (as in *Whitcomb* v. *Brant, supra, Meeker* v. *Spalsbury,* 66 N. J. L. 60, and *Jones* v. *Rushmore*, 67 N. J. L. 157), and a lease which contains no special clause whatever in regard to reletting. In short, a reletting standing alone never effects a surrender under the New Jersey law, but merely constitutes what is called a constructive eviction, the only legal effect of which is to require the landlord to credit the tenant with the avails of reletting.[1]

In every New Jersey case in which it was held that a surrender had been effected, it appeared that something had been said, or something done (other than mere reletting without notice), which was considered inconsistent with the continued relationship of landlord and tenant and which thus evidenced a mutual agreement that the lease should be terminated, such as use of the premises by the landlord for his own purposes (*Lorenz* v. *McCloskey,* 135 Atl. 350; (*Sypherd* v. *Myers,* 80 N. J. L. 321), or the making of alterations by the landlord upon his reentry which completely changed the character of the premises (*Meeker* v. *Spalsbury, supra*) and indicated that the landlord had initiated a venture of his own.

In analyzing the New Jersey decisions it is appropriate that this Court should consider that the presence or absence in a lease of a special clause authorizing reletting has no logical bearing on the question of whether or not the landlord must notify the tenant of his intention to relet for the tenant's account.

[1] For a criticism of the rule that reletting constitutes constructive eviction, see Tiffany, Landlord and Tenant, p. 1276.

Even when there is such a clause in a lease, the landlord, of course, is not obligated to relet as agent for the tenant but may accept the proffered surrender and relet solely for his own account. Consequently, whether or not the lease contains such a covenant, the question in each case is whether the landlord intended to relet for the tenant's account or for his own account.

The most that can be said in favor of the requirement of notice to the tenant that the landlord intends to relet for the tenant's account is that it compels a disclosure of the landlord's intention at the time of reletting. If there is any merit in this requirement it applies equally as well where the lease contains such a clause as where it does not.[1]

It will be observed that, from the point of view least favorable to the petitioner, there is no New Jersey decision holding that a tenant was released merely because the landlord after abandonment relet without notice. Consequently, in that view of the matter, this Court must decide the question of surrender according to its own views of the law of landlord and tenant. *Thorley* v. *Pabst Brewing Co.*, 179 Fed. 338, 339. The rule permitting reletting for the tenant's account, even in the absence of a special covenant, is

[1] If it is relevant that the record in the *Liskovsky* case shows that the lease expressly authorized reletting as agent, then it is also relevant to point out that the record in that case shows that the landlord did *not* notify the tenant that he was reletting for the latter's account, and that there was no evidence as to the landlord's intention in reletting, except the landlord's own testimony that he intended to relet for the tenant's account, although this intention was not communicated to the tenant or to the latter's sureties (State of Case, pp. 80, 97-8). That the court did not attribute importance to the mere undisclosed intention is clearly indicated in its opinion: "* * * There is no proof in the case that plaintiff was acting for the Zimmerman Furniture House, Incorporated [the tenant], when this new lease was made.* * *"

the one which best accords with fairness and public policy.[1]

Whatever could be said for a rule conditioning reletting for the tenant's account upon prior notice to the tenant, there can be no justification for applying such a rule to a corporate tenant which has been adjudicated a bankrupt. The bankrupt corporation, stripped of its assets, would not be concerned with the claim which the landlord would have if the premises should be relet at a loss, or for less than they could have been relet for, and neither the trustee in bankruptcy nor the bankrupt corporation would have the right in New Jersey to recover any over-plus from the landlord if the premises should be relet at a profit, in the absence of a provision in the lease requiring the landlord to account for any such over-plus (*Whitcomb* v. *Brant, supra*). A demand on a bankrupt corporation or its trustee in bankruptcy after rejection for rent or damages would be futile. A notice of reletting for the bankrupt's account would be as little helpful.[2]

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[1] As the Supreme Court of Washington said in *Martin* v. *Siegley, supra*, 123 Wash. 683, 687:

> "It is not in accordance with public policy to lay down a rule whereby the landlord would be required to permit the premises to remain idle over a long term and thereafter recover damages for the full amount of the rentals stipulated for the term, because *it is better for the parties to the agreement, as well as to the public, to have property put to some beneficial use.*"

[2] *Cf.*, the decision of the court below in *In re Mullings Clothing Co.*, 238 Fed. 58, where it was held that a surrender had not been effected under Connecticut law by the landlord's reletting without notice after rejection of the lease by a receiver of the tenant appointed in a dissolution proceeding, although the lease contained no special clause and although no precedent existed under the applicable state law for its decision. In *Miller* v. *Benton*, 55 Conn. 529, cited by the court, it appeared that the landlord twice notified the tenant he would hold him liable for the rent, but no such notice was given in the *Mullings* case.

The Special Master's reasoning in support of his conclusion that a surrender had been accepted (apparently concurred in by the District Court at R. 50) is entirely unsupported, either by authority or principle, and was, as we have seen, rejected by the Court of Appeals:

1. The new lease was not required to recite that the landlord was acting for the tenant (*Liskovsky* v. *Blau, supra*), and no notice was required to be given to the tenant under the authorities cited, which the Master entirely ignored and failed to discuss (R. 40).

2. The Master concluded (R. 40) that because the landlord had no provable claim in bankruptcy it was unlikely for her not to have resumed control of the premises for her own benefit. This presumption of the landlord's intention is inconsistent with the decision of the New Jersey Court of Errors and Appeals in the *Liskovsky* case, where the tenant was also a bankrupt corporation. Moreover, the presumption indulged by the Master is unjustified as a matter of common sense, for there is nothing to justify a presumption that the landlord intended to accept a surrender and terminate the debtor's liability on the lease, since she had nothing to gain by so doing. Under the New Jersey law, even if the landlord succeeds in reletting at a profit, the tenant is not entitled to the profit in the absence of an express provision in the lease (*Whitcomb* v. *Brant, supra*). Thus, in New Jersey there is no reason whatever why the petitioner should have intended to accept a surrender.

3. The Master's conclusion from the filing of a claim for restoration has already been discussed (*supra*, p. 53).

Thus every reason given by the Master for his conclusion is based on an erroneous conclusion of law or an unwarranted assumption of fact. His report and the opinion of the District Court, failing as they do to cite or consider a single New Jersey authority, or, for that matter, any other authority (R. 37-42, 49), are entitled to little weight.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. 260.

IN THE MATTER

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

CITY BANK FARMERS TRUST COMPANY,
Assignee of Florence H. Bugbee,

Petitioner,

against

IRVING TRUST COMPANY, as Trustee of the Estate of the above-named Debtor, *et al.*,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF IN OPPOSITION ON BEHALF OF TRUSTEE

WILLIAM D. WHITNEY,
Counsel for Respondent, Irving Trust Company, as Trustee.

DONALD C. SWATLAND,
R. L. GILPATRIC,
Of Counsel.

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ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF IN OPPOSITION ON BEHALF OF TRUSTEE

OPINIONS BELOW

The opinion of the Special Master (Irwin Kurtz, Referee in Bankruptcy) appears at page 37 of the record and

is not reported. The opinion of the District Court (Judge Hulbert) is found in the record on page 49 and is unofficially reported in CCH Bankrupty Law Service, par. 3702. The opinion of the Circuit Court of Appeals (per Judge Chase) appears on page 71 of the record and is reported in 83 Fed. (2d) 209. All were in favor of respondents.

OUTLINE OF CASE

This Court is asked to review the disallowance, in proceedings under Section 77B of the Bankruptcy Act, of a landlord's claim for loss of future rent after termination of the lease, the landlord having failed to contract for any surviving liability on the part of her tenant in such event. The Special Master found that, upon the disaffirmance of the lease in prior bankruptcy proceedings of the Debtor, the landlord by her own acts had ended the lease and with it all liability of the Debtor long prior to the enactment of Section 77B. On this finding, which was confirmed by the District Court, the Court below held that the landlord had no claim since

> "Sec. 77B did not create new rights to form the basis of claims but only enlarged the remedy to make some valid claims provable in proceedings under Sec. 77B which were not before provable in bankruptcy" (R. 73).

THE FACTS

The lease in question was of premises in the City of Trenton, New Jersey, between the petitioner's assignor (in this brief referred to as the landlord) and the Debtor, for a term which, at the time of the Debtor's adjudication in

bankruptcy on August 29, 1932, had nearly 14 years still to run (R. 19, 20). The Trustee in Bankruptcy found the lease burdensome and, on November 11, 1932, disaffirmed the lease and surrendered the premises (R. 5).

Although the lease made no provision for the Debtor's remaining liable for loss of rent after re-entry upon default, the landlord re-entered immediately (R. 5), restored certain alterations which the Debtor had made (R. 41), and entered into new leases of the property to other tenants (R. 33-35).* So matters stood until Section 77B was enacted over 18 months later, and the Debtor had filed its petition for reorganization thereunder. Then the petitioner, as assignee of the landlord, filed a claim for $86,124.37 representing the whole rent payable under the lease from the Debtor's bankruptcy until expiration, less the alleged fair rental value during the same period (R. 3-10).

QUESTIONS PRESENTED

The Court below was confronted with two questions:

first, whether Section 77B made provable the claim of this landlord who had terminated her lease after its rejection in the prior bankruptcy proceedings of the Debtor, albeit the rejection and termination took place before the enactment of the statute, and

---

*The lease provided that upon default of the tenant "it shall be lawful for the said lessor, without notice, to re-enter the said premises and remove all persons therefrom" (R. 26), and that "at the expiration *or other determination* of this lease" the alterations and improvements to the premises made by the tenant should "belong to and become the property of the lessor" (R. 28).

the lease contained no provision for the Debtor's liability surviving such termination,

and

second, whether the Special Master and the District Court correctly interpreted the New Jersey law in holding that in taking back her property and dealing with it as she did upon the refusal of the Trustee in Bankruptcy to adopt the lease, the landlord had terminated the lease and with it all further liability on the part of the Debtor.

The errors assigned are that in deciding each of these questions against the petitioner the Court below has misconstrued both the federal and the local law. The petitioner also contends that, in taking into consideration on the second branch of the case the effect under the lease and New Jersey law of the landlord's restoration of the premises, the Court below went outside the issues raised by the pleadings or the proof.

STATUTE INVOLVED

The provisions of Section 77B(b) of the Bankruptcy Act dealing with landlords' claims are set forth in Appendix A to this brief.

STATEMENT AS TO THE ISSUE OF FEDERAL LAW PRESENTED

In so far as this case involves the construction of a Federal statute, the precise issue raised is not of general importance, and in deciding it the Circuit Court of Appeals

was astute to interpret the statute so as to avoid doubts as to its constitutionality or conflicts with applicable decisions of this Court. As the petitioner concedes, no conflict has arisen among the several circuit courts of appeals as to the views expressed in the decision below; nor is there any basis that we know of for the petitioner's apprehension that such a conflict will arise in the future.

In fact, this case can only assume importance by treating it, as the petitioner has sought to do, as involving a wide range of questions that *might* arise in the construction of the provisions for landlords' claims in Section 77B.* Actually the one question raised in this case as to the meaning of Section 77B is an exceedingly narrow one, only affecting landlords' claims

> (a) which are based on leases which, *unlike* the ordinary form of lease, contain no special covenants for damage or indemnity, and
>
> (b) where, *prior to* the passage of Section 77B, the liability of the lessee had been terminated during bankruptcy proceedings in which the period for the filing of claims had expired.

In short, the landlords who would benefit from the petitioner's interpretation of the statute are the exception rather than the rule.

In attempting to persuade this Court that there are special and important reasons for a review on writ of certiorari in this case, the petitioner has referred to the status of landlords' claims generally in this reorganization

*See, for example, page 7 of the petition.

proceeding. But, of the 138 landlords' claims filed in this proceeding, totaling $6,185,000, to which the petitioner refers as now pending in various stages of litigation (R. 8), there are but 7 claims, aggregating in amount about $125,000, which would be affected by the granting of a writ in this case. Again, the petitioner charges that the decision below "practically nullifies the obvious attempt of Congress to make provision for landlords' claims" (p. 10); yet the fact is that 170 landlords' claims have been allowed to date in this very proceeding for amounts aggregating over $3,300,000.* Of the 180 other landlords' claims filed against the Debtor and disallowed, the greater part were asserted by landlords who had executed express releases of the Debtor prior to the enactment of Section 77B (see *In re United Cigar Stores Company (Otis)*, 83 Fed. (2d) 202).

In the same vein the petitioner also makes mention of a number of alleged chain store corporations now in reorganization under Section 77B in which the questions involved in the reorganization proceedings of this Debtor are, according to the petition, "certain to arise" (p. 8). Yet there is no specification as to which of such reorganization proceedings grew out of bankruptcy proceedings pending prior to the enactment of Section 77B, nor any showing as to how many claims are pending in such proceedings at the suit of

*It is significant that the petitioner refers in this connection to the decision of the Court below in *In re United Cigar Stores Company (Kuehner and Fischer, appellants)*, not yet reported; whereas the claim in that case, although not provable prior to Section 77B, was actually proved and allowed under Section 77B in the amount of $44,377.55. This was because the claimants' lease, as contrasted with petitioner's lease, did contain a covenant of indemnity against loss which survived the landlords' reentry and termination of the lease.

landlords with leases as deficient as that of the petitioner's with respect to damage or indemnity covenants.

RESPONDENT'S POSITION AND SUMMARY OF ARGUMENT

(a) As to the question of federal law:

The Circuit Court of Appeals has held that Section 77B makes no provision for the allowance of a landlord's claim based on a lease under which the debtor's liability ceased to exist prior to the enactment of the statute, notwithstanding that the lease had been rejected during the debtor's earlier bankruptcy proceedings. This conclusion follows, we believe, not only from the terms of the statute, but also from its purpose and legislative history. Moreover, a contrary interpretation of the statute would, as applied here, raise serious doubts as to its constitutionality.

(b) As to the question of local law:

In affirming the Special Master's findings of fact and ruling on the New Jersey law with respect to surrender, the court below did not so far sanction a departure from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision. On the contrary, in refusing to remand the case on account of a possible technical defect in the pleadings, the Court below was only observing the provisions of Rule XLVII of the General Orders in Bankruptcy promulgated by this Court.

ARGUMENT

I.

THE CIRCUIT COURT OF APPEALS HAS CORRECTLY INTERPRETED SECTION 77B AS NOT EXTENDING THE LIABILITY OF A DEBTOR LESSEE BEYOND WHAT IT WOULD OTHERWISE BE UNDER THE LEASE PROVISIONS AND THE APPLICABLE STATE LAW.

The question of Federal law considered by the Court below was whether, under Section 77B(b), the landlord in this case had "a claim for damages because of injury occasioned by the rejection of the lease by the trustee in the prior bankruptcy proceeding" (R. 72). The question arose in this fashion: After the rejection of the lease in 1932, the Debtor remained as lessee.* Thereupon, the landlord elected to re-enter, restore the premises** and relet to other tenants, these acts together constituting termination of the lease in accordance with its terms and under the applicable New Jersey law.

Thus, at the time Section 77B became law in 1934, there was no obligation owing by the Debtor to the landlord, and the landlord could, therefore, have no claim in these proceedings unless, in enacting Section 77B, Congress had provided a right in bankruptcy where none existed in common law or in equity. The Court below held that this was not the intent of Congress and, we believe, correctly so.

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*See *In re United Cigar Stores Company (Reisenweber's, Inc.)* 69 Fed. (2d) 513, 516-17, C. C. A. 2d., cert. den. 293 U. S. 566.

**In the prior bankruptcy proceedings the landlord was allowed and received dividends upon a claim for expenditures in restoring alterations which the Debtor was obligated to do at the expiration of the term.

(a) The language of the statute discloses no intention to change substantive rights of parties to leases by expanding the liability of the tenant as defined by contract and local law.

Section 77B(b)(10) defines creditors to include

> "all holders of claims of whatever character against the debtor or its property, including claims under executory contracts whether or not such claims would otherwise constitute provable claims under this Act."

The term "claims" is defined in the same section as including

> "debts, securities, other than stock, liens, or other interest of whatever character".

Nowhere in the statute is there any indication that claimants should include others than those to whom the debtor is under some sort of obligation, executory or otherwise, at the time of the filing of the petition for reorganization.

The statute then makes specific reference to landlords' claims as follows:

> "In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor. The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for

> damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63 (a) of this act, * * *."

The petitioner assumes that it comes within the class of landlords "injured by such rejection". It seems apparent, however, that the injury to which the statute refers is legal injury, for which an action would lie against a debtor outside of reorganization proceedings under the statute. Where a word is used in a law, it must have its legal meaning.*

In a brief filed by certain parties as *amici curiae,* an argument is based upon the English law. This overlooks a salient point of distinction between the English law and our bankruptcy jurisprudence as to the effect of the rejection of a lease in a bankruptcy proceeding. Under our law —certainly as it was in 1932 when the rejection in this case took place—the interest in the lease following rejection remains in the bankrupt.** The English Bankruptcy Act, on the other hand, expressly provides that "disclaimer" by the trustee (the equivalent of "rejection" under our nomenclature) shall operate to put an end to all rights and liabilities of the bankrupt as well as the trustee. See Bankruptcy Act of 1914, Section 54 (4 & 5 Geo. V, c. 59).

Moreover, it has long been established in the administration of insolvent estates under the American system that provability of a claim presupposes the existence of a legal right. Thus, the provability of landlords' claims

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*See for example *Ham* v. *State of Missouri,* 18 How. 126, 133; *United States* v. *Fidelity Trust Co.,* 222 U. S. 158, 160.

**Watson* v. *Merrill,* 136 Fed. 359, 363 (C. C. A. 8th); *In re Frazin, et al.,* 183 Fed. 28 (C. C. A. 2nd).

in insolvency proceedings (whether in bankruptcy or equity) require (1) a contract right and (2) recognition of its provability in the particular type of proceedings in question.* Section 77B removed the barrier to provability which formerly existed in the case of landlords' claims for future rent in bankruptcy proceedings (*Manhattan Properties, Inc.* v. *Irving Trust Co.*, 291 U. S. 320). But, as the Court below said in another connection, "there is no new definition of a claim; only of a creditor".**

There is nothing to indicate, therefore, that Congress, in providing for the recognition of landlords' claims,*** intended to do away with the requirement of a contract right or even to make over a landlord's contract by legislating into it a provision, which the landlord himself had failed to insist on, imposing liability on the tenant for future rent after termination. There is no reason why a claim

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*In equity receivership proceedings, provability was recognized when the lease contained a liquidated damage clause (*William Filene's Sons Co.* v. *Weed*, 245 U. S. 597) and, to a limited extent, when there was an ordinary indemnity covenant (*Pennsylvania Steel Co.* v. *New York City Ry. Co.*, 198 Fed. 721, 759, C. C. A. 2nd; *Rogers* v. *United Grape Products*, 2 Fed. Supp. 70, D. C. N. Y.); but not when the lease contained merely a re-entry clause without an indemnity covenant (*Gardiner* v. *William S. Butler & Co.*, 245 U. S. 603).

In ordinary bankruptcy proceedings (prior to the 1934 amendment of Section 63a) only claims based on leases with liquidated damage clauses prevailed (*Irving Trust Co.* v. *A. W. Perry, Inc.*, 293 U. S. 307), ordinary indemnity covenants not sufficing to make the claims provable (*Manhattan Properties, Inc.* v. *Irving Trust Co.*, 291 U. S. 320; *Miller* v. *Irving Trust Co.*, 296 U. S. 256).

***In re United Cigar Stores Company* (*Otis*), 83 Fed. (2d) 202, 206.

***The broad purpose of Section 77B was of course to make the reorganization plan binding on all existing creditors of the debtor corporation, so that the reorganized enterprise would be relieved of the threat of future suits by such creditors. Hence it was necessary that claims formerly non-provable, and hence non-dischargeable by bankruptcy, such as those of tort claimants, and landlords (with legal rights that would otherwise survive against the debtor), should be made provable.

based on a lease should stand on a better footing than any other contract claim. In the absence of a clear expression of legislative intent to the contrary, a landlord's claim "must be adjudged on the basis of the covenant that his interest was inserted in the lease" (*Miller* v. *Irving Trust Co.*, 296 U. S. 256, 258).

Both the petitioner and the *amici curiae* make a point of the language in the statute measuring the landlord's three-year claim from "the date of *surrender of the premises* to the landlord or the date of re-entry of the landlord"; the argument being that by the use of the italicized words Congress must have intended a landlord to have a claim notwithstanding prior surrender of the lease. The defect in this argument lies in a misapprehension of the phrase "surrender of the premises". These words have obviously a meaning different from that of *"surrender of the lease"*, the latter being a technical phrase to describe termination of the landlord and tenant relationship, while the term "surrender *of the premises*" simply indicates the physical turnover of the property necessarily consequent on the rejection of the lease by the trustee in bankruptcy. The technical "surrender" therefore, relates to the *leasehold estate,* while the term used in Section 77B relates only to delivery of the physical premises.

Both briefs in support of the petition also deduce from a change in the language of the bill while it was pending in the Senate that it was the intention of Congress to allow the claim of a landlord even though his lease had been terminated and a surrender accepted after rejection. There was, however, ample reason for the amendments introduced by the Senate, without inferring that they were made for the extraordinary purpose of creating claims where none existed before.*

*See Appendix B for a discussion of this phase of the legislative history of the bill.

(b) By interpreting Section 77B as not creating new claims or taking away valid defenses to claims which existed prior to its enactment, the Circuit Court of Appeals has avoided a grave question as to the constitutionality of the statute.

It is, of course, a familiar canon of construction that

> "A statute must be construed if fairly possible, so as to avoid not only the conclusion that it is unconstitutional but also grave doubts on that score." (*Linder* v. *United States*, 268 U. S. 5, at 17-18.)

In rejecting the petitioner's contention that the statute created new claims for landlords upon rejection of their leases without more, the Court below indicated that it would "have considerable doubt whether the bankruptcy power would support such an effort".* It is true that in *Manhattan Properties, Inc.* v. *Irving Trust Co.* (291 U. S. 320, 332) this Court said that under its bankruptcy power Congress may permit landlords' claims to be proven in bankruptcy proceedings or it may exclude them altogether. This seems to us, however, to mean no more than that Congress may give the character of provability to a valid claim, not that Congress can create claims. But even if Congress *can* (constitutionally) create claims, it would seem that its intention so to do must be expressed in clear and unambiguous language.

Although the courts have never attempted precisely to delimit the bankruptcy power, the decisions from the earliest days have defined it in terms of debtors and their cred-

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*This statement appears in the opinion of the same Court in *In re United Cigar Stores Company* (Kuehner and Fischer, appellants), decided July 14, 1936, and not yet reported.

itors, meaning, of course, existing creditors.* The word "bankruptcy" itself has always referred to the relation of debtors with their creditors (*Continental Illinois National Bank and Trust Co.* v. *Chicago R. I. & Pac. Ry. Co.*, 294 U. S. 648, 672), and thus bankruptcy legislation is primarily concerned with the adjustment of individual rights and liabilities which have their source in local law. Never, however, has the bankruptcy power been exercised to create a new class of obligations of a debtor which would not have existed otherwise.

Moreover, viewed conversely, if Congress has, in enacting Section 77B, created for this landlord a claim in bankruptcy, it has at the same time taken away from the Debtor a valid defense (discharge of liability through termination of the lease). With equal force it could be argued that Section 77B has taken away defenses to claims based on the statute of limitations, or the statute of frauds, or usury. Yet precisely the opposite has been held as regards the provability of claims in ordinary bankruptcy proceedings, although the language of Section 63(a) is open to the same construction. *In re Stern*, 144 Fed. 956 (C. C. A. 8th); *In re German-American Improvement Co.*, 3 Fed. (2d) 572 (C. C. A. 2d); *Remington on Bankruptcy, Fourth Edition*, §§ 1479, 1484.

The contrary would be a strange result for a statute entitled "for the *relief* of debtors". *Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S. 555, at 588:

> "The discharge of the debtor has come to be an object of no less concern than the distribution of his property."

---

*Such cases include *In re Klein*, 1 How. 277 (C. C. Mo.); *In re Reiman*, Fed. Cas. 11,673; *Hanover National Bank* v. *Moyses*, 186 U. S. 181; *Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S. 555, at 582 *et seq.*; and *Continental Illinois National Bank & Trust Co.* v. *Chicago, R. I. & Pac. Ry. Co.*, 294 U. S. 648, 667-674.

It is familiar and fundamental law that a vested defense to a claim or action is fully protected from being cut off or destroyed by subsequent legislative action, whether the defense is based upon a contract or principles of common law. *Pritchard* v. *Norton,* 106 U. S. 124, 132; *Forbes Pioneer Boat Line* v. *Board of Commissioners,* 258 U. S. 338; *P. Ballantine & Sons* v. *Macken,* 110 Atl. 910 (N. J.).

In *Louisville Joint Stock Land Bank* v. *Radford,* 295 U. S. 555, this Court held bankruptcy legislation unconstitutional because it took from a creditor, "without compensation", and gave to the debtor "rights in specific property which was of substantial value". What greater warrant is there for taking away from this Debtor a valid defense to a claim in order to benefit a former creditor, particularly where the donation to the latter is at the expense of the Debtor's *true creditors?*

II.

IT WAS NOT REVERSIBLE ERROR FOR THE SPECIAL MASTER TO INCLUDE IN HIS REPORT A FINDING THAT THE LANDLORD HAD RESTORED ALTERATIONS MADE TO THE LEASED PREMISES BY THE DEBTOR, WHERE THE FACT OF SUCH RESTORATION INDICATED THE TERMINATION OF THE LEASE IN ACCORDANCE WITH ITS PROVISIONS.

(a) The District Court held, and was affirmed by the Court below, following the Special Master, that "the reentry of the landlord under the lease and her subsequent acts terminated all liability on the part of the tenant" (R. 50). The "subsequent acts" were (a) the restoration of the alterations made by the Debtor, which under the lease the

landlord was only free to do at its "expiration or other determination" (R. 28), and (b) the reletting to other tenants without notice to the Debtor. The petitioner's grievance is that of these three acts (*i.e.* the reentry, the restoration and the reletting) only the first and third were referred to in the stipulation of facts entered into by the parties, the facts with regard to the restoration being judicially noticed by the Special Master when he came to prepare his report to the District Court.

There had previously been filed with the Special Master a proof of claim on behalf of this same landlord for expenditures incurred in making the restorations in question. The proof of claim stated that "the lease is now expired by reason of the bankruptcy." Since this proof of claim was, by order of the District Court pursuant to Section 77B(c)(6), made part of the Court records in these proceedings, the Special Master very properly took notice of the allegations made by the landlord therein.

While not denying that the restoration actually took place nor challenging the Special Master's right to take judicial notice of the facts with regard thereto, the petitioner contends that it was improper for such facts to be taken into consideration by the Court below in reaching its decision. The only ground for the petitioner's complaint seems to be that in objecting to its claim on the ground that there had been a forfeiture of the lease, thereby terminating all future obligations of the Debtor thereunder, the Trustee only made specific reference to two of the three evidentiary facts that were the basis of the Special Master's decision, that is, to the reentry and the reletting but not to the restoration (R. 14).

The Court below was not impressed with this rather technical objection and declined to send the case back in

order for the Trustee to plead a fact as to which there was no dispute. We submit that this did not constitute reversible error or grounds for the granting of a writ by this Court, particularly in the light of Rule XLVII of the General Orders in Bankruptcy promulgated by this Court which directs that the reports of special masters in proceedings under Section 77B "shall be deemed presumptively correct" and provides for the modification or rejection of such reports only when the court is *"fully satisfied* that error has been committed".

It is further noteworthy that in excepting to the Special Master's report the petitioner did not assign as error the Special Master's finding that the alterations made by the Debtor had in fact been restored by the landlord, the exceptions going only to the effect given by the Special Master to such restoration (R. 44).

Neither of the cases cited by the petitioner in this connection is in point. In *General Utilities Co.* v. *Helvering,* 296 U. S. 200, the Commissioner of Internal Revenue had raised a question of fact before the Circuit Court of Appeals that had not been presented to or ruled on by the Board of Tax Appeals, although the Court was without power in such a case to make any findings of fact. But in the present case the landlord's conduct in making the restoration was specifically included in the findings of fact of the Special Master, on the basis of which the Court below rendered its decision.

In *Liberty National Bank* v. *Bear,* 265 U. S. 365, the case was remanded because the trustee in bankruptcy, in seeking to invalidate a lien under Section 67f of the Bankruptcy Act, had failed to allege or prove that the debtor was insolvent when the lien was obtained. There is noth-

ing, however, to indicate that this Court would have reached the same conclusion had the Debtor's insolvency been shown by the record (even though not pleaded by the trustee), as is the case here with respect to the restoration of the alterations.

(b) The petitioner also contends that the restoration made by the landlord was in the nature of repairs and that under New Jersey law the making of such repairs does not effect a surrender. Even were this a correct interpretation of the local law, the argument would be of no avail to the petitioner's claim. This petitioner has written her own law in her contract of lease, and it is there provided that it is only upon termination of the lease that she may restore the alterations made by the Debtor.

In any event, the petition admits (at p. 11) that the question of local law is not of sufficient importance in itself to warrant the granting of a writ.

CONCLUSION

The respondent respectfully submits that on the facts of this case the decision below was manifestly correct and in accordance with established principles of law, that no question of great and general interest or importance is presented by this case, and accordingly that no sound reason exists for a review by this Court.

The petition for a writ of certiorari should therefore be dismissed, with costs.

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DONALD C. SWATLAND,
R. L. GILPATRIC,
Of Counsel.

APPENDIX A

Statute Involved.

"The term 'creditors' shall include for all purposes of this section and of the reorganization plan, its acceptance and confirmation, all holders of claims of whatever character against the debtor or its property, including claims under executory contracts whether or not such claims would otherwise constitute provable claims under this Act. The term 'claims' includes debts, securities, other than stock, liens, or other interests of whatever character. * * * In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor. The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63 (a) of this act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or reentry: * * *." Bankruptcy Act § 77B (b) (10), 11 U. S. C. A. Sec. 207 (b) (10).

APPENDIX B

Statement as to Certain Aspects of Legislative History of Section 77B

The bill (H. R. 5884), as it was originally passed by the House, provided in respect of landlords' claims as follows:

> "In case any executory contract shall be rejected, the same shall be deemed to have been breached [as of the date of the approval of the petition or answer filed], and the holder shall be entitled to file a claim for damages for such breach, and such claim may be allowed provided such contract shall not have been terminated by forfeiture, reentry or otherwise." (Matter in brackets ours.)

This provision was changed by an amendment on the floor of the Senate to a form substantially similar to that finally adopted, viz.:

> "In case any executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee in bankruptcy or receiver in equity in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor to the extent of the injury resulting from such rejection * * *."

The original phrasing clearly had to be discarded, for it was insufficient from the landlord's point of view in two important respects:

First, the typical lease* contains a covenant for damages or indemnity after termination, and the reference in the original statutory phrasing to every "holder" of an executory contract might well have been construed to cover every holder of such a covenant, with the consequence that claims on the covenants themselves would have been lost by termination.**

Second, the original phrasing was wholly inapplicable to pending bankruptcy or equity receivership proceedings.

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*Represented, for example, by 331 out of the 354 leases on which proofs of claims were filed in the present proceedings.

**Such a rule would in fact have eliminated cost of the landlords' claims which have been allowed in this very proceeding.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. 260.

IN THE MATTER

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor,

CITY BANK FARMERS TRUST COMPANY,
Assignee of Florence H. Bugbee,

Petitioner,

against

IRVING TRUST COMPANY, as Trustee of the Estate of the above-named Debtor, *et al.*,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI.

SUPPLEMENTAL BRIEF IN OPPOSITION

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SUPPLEMENTAL BRIEF IN OPPOSITION

This supplemental brief is filed only because the petitioner has filed a "reply brief" in which it charges that our brief contained erroneous or misleading statements of fact. These occur in the paragraphs of the "reply brief"

numbered (1), (2) and (7) and are here answered *seriatim*.

(1) *As to the questions presented by the petition:* In our original brief herein we did not and could not anticipate the questions under Section 77B sought to be raised by the petition in the *Kuehner* case (Docket No. 354), which was not filed until *after* our brief in this case was served. The Trustee's position with respect to those questions will be set forth in its brief in opposition to the *Kuehner* petition. For a statement of the sole questions presented in this case we respectfully refer the Court to pages 3 and 4 of our original brief.

(2) *Other claims affected by this case:* We stand on the statement in our original brief (p. 6) that of the other landlords' claims being litigated in this proceeding there are not more than 7, aggregating in amount about $125,000, which would be affected by the granting of a writ in this case. As to the bulk of the claims in litigation, petitioner's counsel themselves urged a distinction upon the court below in that, as contrasted with petitioner's assignor, such claimants had

> "*by express agreement* with United and others voluntarily extinguished all liability of United and its estate on the lease".

The only other landlords' claims still pending are those where, as in the case of the *Voigt* claim represented by the *amici curiae*, the landlord claimant had terminated the lease *before* the trustee in bankruptcy had exercised its election to adopt or reject. Such a claimant can hardly establish

a claim "for injury arising from the rejection" of a lease, at least not under the theory advanced by this petitioner whose assignor did not terminate until *after* rejection.

(7) *The Special Master's finding on restoration:* Any doubts as to the force of the Special Master's finding on the subject of the restoration of the Debtor's alterations made by the petitioner's assignor can best be settled by reference to the Special Master's own language (R. 41, 42):

> "As bearing on the Landlord's present contention, it might be well to note that she filed in the Bankruptcy proceeding, a claim for $1980.99 for alleged expenditures in restoring a party wall and closing up a common entrance in the demised premises, based upon the United's agreement to restore the demised premises *at the expiration of the term.* She received 50% dividends in the Bankruptcy proceeding, and the stipulation herein shows that this claim is also asserted in this Reorganization proceeding. Naturally, the entire basis of this claim for restoration is the expiration of the lease. The Trustee may well point to it, as showing that the Landlord, prior to the enactment of Section 77-B, by her re-entry and reletting of the premises as aforesaid, considered that the lease terminated and expired. It is significant also to note that the lease contained no provision giving the Landlord the right to re-enter for the purpose of reletting for the account of the Tenant.
>
> "All in all, the conclusion is irresistible from the Landlord's entire course of conduct, after the adjudication in bankruptcy herein on August 29th, 1932, that she in fact regarded the lease terminated, and that she reentered the premises and resumed control thereof solely for her own account."

Inasmuch as the other points dealt with in the reply brief involve questions of law, we rest as to them on the arguments in the Trustee's original brief.

Respectfully submitted,

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Supreme Court of the United States

OCTOBER TERM, 1936.

No: 260.

IN THE MATTER

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ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR RESPONDENT TRUSTEE

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Supreme Court of the United States

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Respondents.

No. 260.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR RESPONDENT TRUSTEE

OPINIONS BELOW

The opinion of the Special Master appears at page 37 of the record and is not reported. The opinion of the District Court is found in the record at page 49 and is unofficially reported in CCH Bankruptcy Law Service, par. 3702. The opinion of the Circuit Court of Appeals appears on page 71 of the record and is reported in 83 Fed. (2d) 209. All were in favor of respondents.

STATUTE INVOLVED

The provisions of Section 77B (b) of the Bankruptcy Act dealing with landlords' claims are set forth in the Appendix to this brief.

OUTLINE OF CASE

This Court is asked to review the disallowance, in proceedings under Section 77B of the Bankruptcy Act, of a landlord's claim for loss of future rent after termination of the lease, the landlord having failed to contract for any surviving liability on the part of her tenant in such event. The Special Master found that, upon the disaffirmance of the lease in prior bankruptcy proceedings of the Debtor, the landlord by her own acts had ended the lease and with it all liability of the Debtor long prior to the enactment of Section 77B. On this finding, which was confirmed by the District Court, the Court below held that the landlord had no claim since

> "Sec. 77B did not create new rights to form the basis of claims but only enlarged the remedy to make some valid claims provable in proceedings under Sec. 77B which were not before provable in bankruptcy" (R. 74).

THE FACTS

The lease in question was of premises in the City of Trenton, New Jersey, between the petitioner's assignor (in this brief referred to as the landlord) and the Debtor, for a term which, at the time of the Debtor's adjudication in bankruptcy on August 29, 1932, had nearly 14 years

still to run (R. 19, 20). The Trustee in Bankruptcy found the lease burdensome and, on November 11, 1932, rejected the lease and surrendered the premises (R. 5).

Although the lease made no provision for the Debtor's remaining liable for loss of rent after re-entry upon default, the landlord re-entered immediately (R. 5), restored certain alterations which the Debtor had made (R. 41), and entered into new leases of the property to other tenants, certain of whom were formerly sub-tenants of the Debtor (R. 33-35).[1]

So matters stood until Section 77B was enacted over 18 months later, and the Debtor had filed its petition for reorganization thereunder. Then the petitioner, as assignee of the landlord, filed a claim for $86,124.37 representing the whole rent payable under the lease from the Debtor's bankruptcy until expiration, less the alleged fair rental value during the same period (R. 3-10).

QUESTIONS PRESENTED

The Court below was confronted with two questions: *first*, whether Section 77B made provable the claim of this landlord who had terminated her lease after its rejection in the prior bankruptcy proceedings of the Debtor, albeit the rejection and termination took place before the enactment of the statute, and the

---

[1]The lease provided that upon default of the tenant "it shall be lawful for the said lessor, without notice, to reenter the said premises and remove all persons therefrom" (R. 26), and that "at the expiration *or other determination of this lease*" the alterations and improvements to the premises made by the tenant should "belong to and become the property of the lessor" (R. 28).

lease contained no provision for the Debtor's liability surviving such termination,

and

second, whether the Special Master and the District Court correctly interpreted the New Jersey law in holding that in taking back her property and dealing with it as she did upon the refusal of the Trustee in Bankruptcy to adopt the lease, the landlord had terminated the lease and with it all further liability on the part of the Debtor.

The errors assigned are that in deciding each of these questions against the petitioner the Court below has misconstrued both the federal and the local law. The petitioner also contends that, in taking into consideration on the second branch of the case the effect under the lease and New Jersey law of the landlord's restoration of the premises, the Court below went outside the issues raised by the pleadings or the proof.

The first issue is a narrow one. Its determination only affects landlords' claims which are

(1) against tenants with respect to whom bankruptcy proceedings were pending *prior to* the passage of Section 77B, and

(2) based on leases which, unlike the ordinary form of lease, contain no special covenants for damage or indemnity, and in which the landlord had, during the prior bankruptcy proceedings, re-entered or otherwise terminated his rights.

In other words, the decision below leaves intact the provability of all claims that may arise or exist in the future, and as to claims under leases that were rejected during a prior bankruptcy proceeding, leaves intact those of landlords

(1) who had not re-entered or otherwise terminated prior to their tenants' filing under Section 77B, or

(2) whose leases had terminated prior to the time of such filing, but who either

(i) had independent damage covenants, or

(ii) had independent indemnity covenants.

Of the 354 claims filed by landlords in these proceedings, only 23 (including this claim) were based on leases which lacked indemnity or damage covenants. Of these, some had preserved their rights by refraining from re-entry, or by re-entering in accordance with the terms of their leases or applicable state law in such a manner as not to waive their claims against the Debtor. There are still pending the claims of 7 landlords (including this claimant) who had re-entered, or otherwise terminated their leases, without taking the necessary statutory or contractual procedure to retain claims; these 7 claims aggregate about $125,000 on the statutory three-year rental basis.

The question which this Court is called upon to decide can only arise where it is necessary to give Section 77B *retroactive* operation.

SUMMARY OF ARGUMENT

I

The bulk of petitioner's brief is directed to an interpretation of the provisions in Section 77B as applicable to a rejection of a lease *subsequent to* the enactment of the statute. It is then *assumed* that, if a rejection subsequent to the statute is to have certain legal effects, a rejection in a bankruptcy proceeding prior to the enactment of the statute must now be deemed to have had the same effects, quite regardless of anything that has happened in the interim. In this case, the rejection was over a year and a half before the enactment of Section 77B and the commencement of proceedings by the Debtor thereunder, and in the interim the petitioner's assignor terminated her lease without reservation or qualification (or at least we must so assume for the purpose of this argument).

At the time of the rejection, the landlord of course had a claim against the Debtor, in the sense that the Debtor continued liable under all of the terms of the lease. But that claim was ended by the termination of the lease.

The single question in the case is whether Congress intended to, or constitutionally could, revive an extinct claim. This is of course the same as to create a claim where none exists.

So extraordinary an intention may not be imputed to Congress in the absence of compelling language to the contrary. No such language appears in this statute.

And it is well established in the administration of insolvent estates under our system that provability of a claim presupposes the existence of a legal right. The subject matter of bankruptcy is the relationship of debtors and

creditors, the equitable distribution of estates among creditors, and the relief of debtors. None of these ends calls for the creation of new claims or for the revival of dead claims. References by the petitioner to the English statute are irrelevant, as that statute is prospective in operation only and does not touch upon the question here presented.

Nor is there any evidence in the legislative history of Section 77B to the contrary

By interpreting Section 77B as not creating new claims, or taking away valid defenses to claims which had once existed but ceased to exist prior to its enactment, the Circuit Court of Appeals has avoided a grave question as to the constitutionality of the statute.

II

Incidental questions are presented (1) as to whether the courts below correctly construed the New Jersey law, in determining that the unqualified reentry, reletting and restoration of the leased premises by the landlord terminated the lease, and (2) whether the Circuit Court of Appeals committed reversible error in basing a finding (as to the landlord's action in restoring alterations) upon a statement in the report of the Special Master.

As to New Jersey law, it is assumed that this Court will be reluctant to construe the state court cases contrary to the construction unanimously put upon them by the courts below. It appears that New Jersey belongs to that minority of states in which mere reentry does not by itself constitute a surrender and termination, but it further appears that, where the landlord has made substantial alterations in the premises for the purpose of restoration, the result is to effect a surrender by operation of law. And in this case,

the lease specifically provided that alterations and/or improvements should become the property of the lessor at the expiration or other termination of this lease. By a restoration of the premises to their original condition, the landlord clearly evidenced her understanding that the relation of landlord and tenant was at an end.

The facts as to the restoration appear in the record in the Special Master's report. The petitioner had filed a claim in the prior bankruptcy proceedings for her expenses in making the restoration. And the Special Master's report, by Rule XLVII of the General Orders of Bankruptcy, is deemed presumptively correct, and will not be reversed unless the Court is fully satisfied that error has been committed. There has been no suggestion, either by exception to the Master's report, assignment of error on appeal, or in the brief to this Court, that the petitioner had not made the restoration in question, and the point is therefore without substance.

ARGUMENT

I

THE CIRCUIT COURT OF APPEALS HAS CORRECTLY INTERPRETED SECTION 77B AS NOT CREATING A CLAIM AGAINST THE DEBTOR WHERE NONE WOULD OTHERWISE HAVE EXISTED UNDER THE LEASE PROVISIONS AND THE APPLICABLE STATE LAW.

The question of federal law considered by the Circuit Court of Appeals was whether, under Section 77B(b), the landlord in this case had "a claim for damages because of injury occasioned by the rejection of the lease by the trus-

tee in the prior bankruptcy proceeding" (R. 72). The question arose in this fashion: After the rejection of the lease in 1932 the Debtor remained as lessee. *In re United Cigar Stores Co. (Reisenweber's, Inc.)*, 69 Fed. (2d) 513, 516-517 (C. C. A. 2d), cert. den. 293 U. S. 566. Thereupon the landlord elected to reenter, restore the premises and relet to other tenants, these acts together constituting termination of the lease in accordance with its terms and under the applicable New Jersey law.[2]

Thus at the time Section 77B became law in 1934, there was no obligation owing by the Debtor to the landlord, and the landlord could, therefore, have no provable claim in these proceedings unless in enacting Section 77B Congress had, by the use of the words "injury resulting from the rejection of an unexpired lease", provided a remedy in bankruptcy where no right existed in common law or in equity.

(A) There is nothing in the language, background or legislative history of the statute which discloses an intention to create substantive rights where none existed at the time of its enactment.

1. The statutory language.

Section 77B(b)(10) defines creditors to include

> "all holders of claims of whatever character against the debtor or its property, including claims under executory contracts whether or not such claims would otherwise constitute provable claims under this Act."

The term "claims" is defined in the same section as including

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[2]See discussion under Point II, *infra*, p. 22.

> "debts, securities, other than stock, liens, or other interest of whatever character".

The statute then makes specific reference to landlords' claims as follows:

> "In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor. The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63 (a) of this act, * * *."

The injury to which the statute refers must be legal injury, for which an action would lie against a debtor outside of reorganization proceedings under the statute. Where a word is used in a law, it must have its legal meaning. See *Ham* v. *State of Missouri*, 18 How. 126, 133; *United States* v. *Fidelity Trust Co.*, 222 U. S. 158, 160.

When the Section 77B petition was filed, the petitioner's assignor was not a sufferer from any legal "injury", as she had no legal claim whatsoever.

The petitioner must argue, therefore, that the statute was intended to eradicate past forfeitures and surrenders, to revive dead claims, and to nullify defenses thereto.

So remarkable a view would seem to require compelling language in the statute for its support. But the only language found by the petitioner is the use of the word "re-entry" in the next sentence of the statute:

> "The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with defendants which would be provable under §63 (a) of this Act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of *the surrender of the premises* to the landlord or the date of *re-entry* of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or re-entry * * *." (Italics ours.)

The argument from the use of this word "re-entry" is that it connotes termination, and that Congress would not have used a word of termination as a basis for measuring claims if Congress intended claims to be obliterated by termination.

There are many difficulties with the argument. *First,* Congress could hardly have used a more indirect, artificial and disingenuous method of expressing an intention so extraordinary as the revival of a dead claim. *Second,* Congress presumably did not use the word "re-entry" in its technical sense to indicate termination, because it is coupled with the phrase "surrender of the premises", which the petitioner quite properly concedes to be a word expressive of a mere physical act rather than of a legal concept. In other words, Congress was simply measuring the limita-

tion on landlords' claims in a very practical way from the date on which the physical turnover of property would be made consequent upon rejection. *Third*, the word "reentry", even if used in a technical sense, would not necessarily connote termination, as there are some states in which reentry alone does not constitute termination. This is best evidenced by the fact that petitioner's second argument in this case is that, although its assignor concededly reentered, she did not thereby terminate.

The question whether Congress did intend that "in the future rejection should have the effect of termination, will be a question of major importance that may arise to be considered in some future case under Section 77B; but it is not presented at all in this case, as here the reentry took place long prior to the enactment of Section 77B. Accordingly, the only question in this case is whether Congress intended to revive a claim concededly dead. Such an intention would be so extraordinary as to require language far more compelling than is evidenced by the tucking away in the subordinate measurement clause of the word "reentry".

2. The background of the statute.

It has long been established in the administration of insolvent estates under the American system that provability of a claim presupposes the existence of a legal right. Thus, for a landlord to establish a claim in an insolvency proceeding (whether in bankruptcy or in equity), he has always been required to prove (i) a contract right or cause of action under the substantive law of landlord and tenant and (ii) recognition of such right or cause of action in the particular type of proceedings in question.

In equity receivership proceedings, provability was recognized when the lease contained a liquidated damage clause (*William Filene's Sons Co. v. Weed*, 245 U. S. 597) and, to a limited extent, when there was an ordinary indemnity covenant (*Pennsylvania Steel Co. v. New York City Ry. Co.*, 198 Fed. 721, 759; *Western Electric Company, Inc. v. Powers Accounting Machine Company, Claim of Pren-Brook Corp.*, unreported memorandum opinion by Mack, C. J., April 14, 1922; *Rogers v. United Grape Products*, 2 Fed. Supp. 70); but not when the lease contained merely a re-entry clause without an indemnity covenant (*Gardiner v. William S. Butler & Co.*, 245 U. S. 603).

In ordinary bankruptcy proceedings (prior to the 1934 amendment of Section 63a) only claims based on leases with liquidated damage clauses prevailed (*Irving Trust Company v. J. W. Perry, Inc.*, 293 U. S. 307), ordinary indemnity covenants not sufficing to make the claims provable (*Manhattan Properties, Inc. v. Irving Trust Co.*, 291 U. S. 320; *Miller v. Irving Trust Co.*, 296 U. S. 526).

As this Court said in the case last cited (which also involved a New Jersey lease), the landlord's claim

> "must be adjudged on the basis of the covenant that in his interest was inserted in the lease".

Admittedly Section 77B removed the barrier to provability which formerly existed in the case of landlords' claims for future rent in bankruptcy proceedings (*Manhattan Properties, Inc. v. Irving Trust Co.*, 291 U. S. 320). But there is nothing to indicate that Congress intended to re-make the agreement between the parties for the purposes of the federal Bankruptcy Act, or (to use the language of

petitioner's brief, at p. 20) "that the technical law of landlord and tenant of the states should not be applied in the administration of the federal bankruptcy law" under Section 77B.

Certainly, if Section 77B was supposed "to do away for the purpose of the bankruptcy law with the historical distinction between leases and other types of obligations" (petitioner's brief, p. 42), Congress should have so declared in clear and unambiguous language (*Maynard* v. *Elliott*, 283 U. S. 273, 277).

The petitioner and the *amici curiae* say that at the time of enacting Section 77B Congress had in mind the language of the English bankruptcy acts making landlords' claims for loss of future rent provable.[3] This is an argument similar to the argument based on the use of the word "reentry" (*supra*, p. 11), in that here again the petitioner's purpose is to show that Congress intended that a rejection in the future should have the same effect as a termination. But this again is irrelevant to the question whether Congress intended to revive, or could constitutionally revive, a dead claim. Petitioners do not suggest that even the English statute attempted to revive dead claims, or otherwise to clothe a previously consummated act with legal effects different from that which it had at the time that it occurred.

When this Court is presented with the question whether a rejection of a lease has all the legal effect of a termination, it will no doubt be relevant to consider the English statute.[4]

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[3]Petitioner's brief, at page 14; *amici curiae* brief, at page 15.

[4]And it will then incidentally appear that the English statute is quite different from our statute in that it contains an *express* provision that "disclaimer" (the nearest English equivalent to our "rejection") operates to put an end to all

3. The purpose and legislative history of Section 77B.

Not merely is there no evidence on the face of the statute or in its background to support the petitioner's theory of legislative intent, but it is contrary to the expressed purpose of the sponsors of the statute.

Senator Hastings, who had charge of the bankruptcy amendments, stated that future rent claims would be provable

> "because we have undertaken in these sections to include all the claims that could be had against a debtor, so that when he got relief he might know that he had relief from every kind of a claim that might be had against him." [76 Cong. Rec. 4906]

The emphasis upon relief against actual claims, and the absence of even an implied intent to add to existing claims, is apparent.

The petitioner relies upon a change which the Senate itself made in the House bill. The bill (H. R. 5884, 73rd Cong., 1st Sess.), as it was originally passed by the House, contained a provision looking solely to the future, and substantially similar to the English provision, as follows:

> "In case any executory contract shall be rejected, the same shall be deemed to have been breached [as of the date of the approval of the petition or answer filed], and the holder shall be entitled to file a claim for damages for such breach, and such claim may

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rights and liabilities of the bankrupt as well as the trustee. 4 and 5 Geo. V (c) 59. Under our statute (prior to Section 77B), the interest in the lease following rejection remains in the bankrupt (*Watson* v. *Merrill*, C. C. A. 8th, 136 Fed. 359, 363; *In re Frazin*, C. C. A. 2d, 183 Fed. 28) and Section 77B contains no such express provision.

> be allowed provided such contract shall not have been terminated by forfeiture, re-entry or otherwise." (Matter in brackets ours.)

This provision was changed by an amendment on the floor of the Senate to a form substantially similar to that finally adopted, viz.:

> "In case any executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee in bankruptcy or receiver in equity in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor to the extent of the injury resulting from such rejection. * * *" (78 Cong. Rec. 8109).

The change was essentially two-fold, (1) application to prior pending bankruptcy proceedings as well as to future proceedings, offset by (2) elimination of the explicit provision as to the effect of rejection and its replacement by the simpler formula that those who are "injured" may recover. That formula left to existing law the determination of who is "injured". But, concededly, under existing law this petitioner was not an "injured" person when the statute was enacted or when it was applied to this estate.

And the original phrasing was insufficient from the landlord's point of view in two important respects:

First, the typical lease[5] contains a covenant for damages or indemnity after termination,[6] and the reference in the original statutory phrasing to every "holder" of an executory contract might well have been construed to cover every holder of such a covenant, with the consequence that claims on the covenants themselves would have been lost by termination.

Second, the original phrasing was wholly inapplicable to pending bankruptcy or equity receivership proceedings.

Judge Learned Hand of the Circuit Court of Appeals had the following to say in the *Kuehner and Fischer* case, No. 354 here, with regard to the petitioner's argument that this change indicated an intention on the part of Congress to grant a claim for rejection to a landlord regardless of the termination of his lease (85 Fed. (2d) 35, 37):

> "At least the original bill attempted nothing of the sort, and a change of language so inartificial and obscure ought not, it seems to us, be given so extravagant an effect. It is not necessary to read it so; it is enough if the language be taken to mean that the 'rejection' of a lease shall be a present breach of all the lessee's promises, either to pay rent, to rebuild, to cover taxes or whatever else they may be. Indeed, if it continues his liability after reentry, it was redundant to include covenants 'for damages or indemnity'. We do not therefore believe that this language creates new claims after reentry, * * *."

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[5]Represented, for example, by 331 out of the 354 leases on which proofs of claims were filed in the present proceedings. See [redacted] page 5.

[6]See *Manhattan Properties, Inc.* v. *Irving Trust Co.*, 291 U. S. 320, 337 *et seq.*

There was, therefore, ample reason for the amendments introduced by the Senate, without inferring that they were made for the extraordinary purpose of reviving claims which the parties themselves had terminated or forfeited. Indeed, it seems obvious that when a brief statutory provision having only *prospective* operation is expanded and altered so as to cover *retrospective* application as well, inferences cannot be drawn from the precise phrasing of the former for the purpose of giving a distorted construction to the latter.[7]

(B) *By interpreting Section 77B as not creating new claims, or taking away valid defenses to claims which had once existed but had ceased to exist prior to its enactment, the Circuit Court of Appeals has avoided a grave question as to the constitutionality of the statute.*

It is, of course, a familiar canon of construction that

> "A statute must be construed if fairly possible, so as to avoid not only the conclusion that it is unconstitutional but also grave doubts on that score." (*Linder* v. *United States,* 268 U. S. 5, at 17-18.)

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[7]One commentator (Mr. Henry Friendly) has said of the change (48 Harv. L. R. 39, 65):

> "But the amendment also changed the bill in other respects, notably in limiting the amount of the landlord's claim, and there is nothing either in the language of the Act or in the debates that shows an intention to confer on a landlord the right to prove a claim in a case where he would never have been able to sustain an action at law."

To the same effect is the report, dated June 12, 1935, of former Judge Thomas D. Thacher, sitting as Special Master in the reorganization proceedings of Radio-Keith-Orpheum Corporation (D. C. S. D. N. Y., unreported).

Concededly, this landlord had, on the day previous to the filing of the Debtor's petition under Section 77B, no claim either against the bankrupt estate of the Debtor or against the Debtor itself. Against the estate the landlord had no claim because of the ruling in the *Manhattan Properties* case (291 U. S. 320). Against the Debtor she had none because she had previously terminated her lease.

This Court said in the *Manhattan Properties* case, 291 U. S. 320, at page 332, that under its bankruptcy power Congress may permit landlords' claims to be proven in bankruptcy proceedings or it may exclude them altogether. This seems to us, however, to mean no more than that Congress may give the character of provability to a valid claim, not that Congress can (constitutionally) create claims.

Although the courts have never attempted precisely to delimit the bankruptcy power, the decisions from the earliest days have defined it in terms of debtors and their creditors, meaning, of course, existing creditors.[8] The word "bankruptcy" itself has always referred to the relation of debtors with their creditors (*Continental Illinois National Bank and Trust Co.* v. *Chicago, R. I. & Pac. Ry. Co.*, 294 U. S. 648, 672), and thus bankruptcy legislation is primarily concerned with the adjustment of individual rights and liabilities which have their source in local law. Never, however, has the bankruptcy power been exercised to create a new class of obligations of a debtor which would not have existed otherwise.

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[8]Such cases include *In re Klein*, 1 How. 277 (C. C. Mo.); *In re Reiman*, Fed. Cas. 11,673; *Hanover National Bank* v. *Moyses*, 186 U. S. 181; *Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S. 555, at 582 *et seq.*; and *Continental Illinois National Bank & Trust Co.* v. *Chicago, R. I & Pac. Ry. Co.*, 294 U. S. 648, 667-674.

Moreover, viewed conversely, if Congress has, in enacting Section 77B, created for this landlord a claim in bankruptcy, it has at the same time taken away from the Debtor a valid defense (discharge of liability through termination of the lease). With equal force it could be argued that Section 77B has taken away defenses to claims based on the statute of limitations, or the statute of frauds, or usury. Yet precisely the opposite has been held as regards the provability of claims in ordinary bankruptcy proceedings, although the language of Section 63(a) is open to the same construction. *In re Stern*, 144 Fed. 956 (C. C. A. 8th); *In re German-American Improvement Co.*, 3 Fed. (2d) 572 (C. C. A. 2d); *Remington on Bankruptcy, Fourth Edition*, §§ 1479, 1484.

The contrary would be a strange result for a statute entitled "for the *relief* of debtors". *Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S. 555, at 588:

> "The discharge of the debtor has come to be an object of no less concern than the distribution of his property."

It is familiar and fundamental law that a vested defense to a claim or action is fully protected from being cut off or destroyed by subsequent legislative action, whether the defense is based upon a contract or principles of common law. *Pritchard* v. *Norton*, 106 U. S. 124, 132; *Forbes Pioneer Boat Line* v. *Board of Commissioners*, 258 U. S. 338; *P. Ballantine & Sons* v. *Macken*, 110 Atl. 910 (N. J.). This rule applies here where the defense—surrender by operation of law—"did something more than resist the remedy"; it "disproved the right of action" (*Winfree* v. *Northern Pacific Ry. Co.*, 227 U. S. 296, 302). Indeed, courts endeavor to hold inapplicable even changes in the

form of remedies, "where the effect is to reach backward and nullify by relation the things already done." (Cardozo, *J.*, in *Matter of Berkovitz* v. *Arbib & Houlberg*, 230 N. Y. 261, 270.) See also *U. S. Fidelity & Guaranty Co.* v. *Struthers-Wells Co.*, 209 U. S. 306.

Finally, there is still another serious constitutional question presented if, by the use of the words "injury resulting from rejection", Congress gave to the act of the Debtor's trustee in bankruptcy, in rejecting the petitioner's lease in 1932, a consequence it was not intended to have and did not have at the time. As this Court has held,

> "A statute having such a result may incur the opposition of the Constitution. When such may be the result a different construction of the statute is determined." (*Union Pacific R. R. Co.* v. *Laramie Stock Yards Co.*, 231 U. S. 190, 200.)

The same would be true of any statute enacted under a federal power if "construed retroactively to create liability". *William Danzer Co.* v. *Gulf, etc. R. R.*, 268 U. S. 633, 637:

> "To give it that effect would be to deprive defendant of its property without due process of law in contravention of the Fifth Amendment".

The converse of the situation here presented arose in *Auffm'ordt* v. *Rasin*, 102 U. S. 620, where this Court stated, referring to an amendment of the Bankruptcy Act changing from four to two months the period within which preferential transfers should be voidable:

> "But this statute is not a statute of limitation of actions, but a declaration of a period when an act otherwise voidable shall be held to be valid; and we

> see no reason to believe that in making a new rule on that subject Congress intended to make it retrospective, for the purpose of destroying rights of property or rights of action which had become vested before the passage of the law."

The petitioner argues that when a Debtor has voluntarily filed a petition under Section 77B, the Trustee of its estate is estopped to suggest that grave constitutional doubts be avoided in the interpretation of the statute. The argument is that a person cannot avail himself of the benefits of a statute and at the same time seek to escape its burdens. But the very point here at issue is whether the statute intends the Debtor to be subjected to the burdens for which the petitioner contends. In the three cases cited by the petitioner (brief, p. 38), direct assaults on the validity of the statutes in question were made by those who had accepted benefits under them; not so in this case. Far from asserting the unconstitutionality of Section 77B or any part of it as it stands, the respondent's sole effort is to *avoid* any question of its constitutionality being raised now or in the future by the adoption of the strained interpretation urged by the petitioner.

II

BY HER UNQUALIFIED REENTRY, RELETTING AND RESTORATION OF THE LEASED PREMISES IN NOVEMBER, 1932, THE LANDLORD TERMINATED THE LEASE AND ENDED ALL FURTHER LIABILITY OF THE DEBTOR THEREUNDER.

The petitioner does not dispute that if a surrender of the lease by operation of law did take place in November,

1932, no liability of the Debtor to the landlord for rent to accrue thereafter would have survived. New Jersey follows the common law rule in effect in most states that where, as here, the lease contains no indemnity covenant or damage clause, a surrender extinguishes all further liability of the tenant. See *Fleming* v. *Matter Const. Corp.*, 164 Atl. 585, at 586 (N. J.); and annotations in 18 A. L. R. 957, at 960, and 58 A. L. R. 906.

(A) *The landlord's acts indicated an acceptance of surrender.*

The actual conduct of the landlord in this case is not disputed, and there was presented no evidence of her intention other than that to be inferred from her acts. Immediately after the Debtor's Trustee in Bankruptcy rejected the lease and abandoned the premises in November, 1932, the landlord reentered and proceeded to make new leases with other tenants for various portions of the premises (R. 20, 33-35). Some of these new leases were with others than the former subtenants of the Debtor, and several were for long terms. No notice was given by the landlord to the Debtor (or indeed to the Trustee in Bankruptcy), either of intention to relet the premises for the benefit of the Debtor, or of the reletting itself. A final determinative indication of the landlord's understanding that she was quit of the Debtor as a tenant and that the lease was completely at an end, is her action, as found below, in restoring structural alterations that had been made to the premises by the Debtor, which under the lease she was not free to do until its "expiration or *other determination*" (R. 28).

The first intimation that the landlord chose to consider the Debtor as remaining liable for rent accruing after she

had taken back the premises, was the filing of the claim which is the subject of this appeal. This was on October 10, 1934, nearly two years after the landlord-tenant relationship had evidently come to an end.

(B) *Under New Jersey law the Debtor's liability as tenant did not survive in this case.*

Although there are several different theories as to how a landlord whose lease contains no indemnity covenant may reenter the demised premises without discharging the tenant from liability on the lease, the rule that is almost universally followed is the common-law rule that reletting by the landlord without intent to hold or to act for the account of the tenant effects a surrender. See extensive annotations in 3 A. L. R. 1080; 52 A. L. R. 154 and 61 A. L. R. 773.

In New Jersey the rule is stated as follows:

> "The essentials of this recognized mode by which the relation of landlord and tenant may be terminated were stated by Mr. Justice Collins in the case of *Mecker* v. *Spalsbury,* 37 Vroom 60, and the statement there made was approved and adopted by this court in the more recent case of *Miller* v. *Dennis,* 39 *Id.* 320. The text is: 'When the minds of the parties to a lease concur in the common intent of relinquishing the relation of landlord and tenant and execute this intent by acts which are tantamount to a stipulation to put an end thereto, there at once arises a surrender by act and operation of law.'" (*Syphcrd* v. *Myers,* 80 N. J. L. 321, 324.)

The same case further clarifies the rule:

> "That the giving up of possession to the landlord, if acted upon by him, is such an act is the established rule tersely stated by Mr. Justice Tindal

> in *Dodd* v. *Acklom*, 6 M. & G. 672: 'A change of possession by the consent of both parties amounts to a surrender by operation of law.' "[9]

It is apparent that in New Jersey an unqualified resumption of possession and a reletting by a landlord, especially when accompanied by alterations in the premises, as in the present case, constitute a surrender. *Sypherd* v. *Myers, supra; Fink* v. *Browe Co.* (N. J. C. H.), 99 Atl. 926; *Miller* v. *Dennis*, 53 Atl. 394, cited in *In re Sherwoods*, 210 F. 754, 759.

Indeed, the holding in *Fink* v. *Browe Co., supra*, is based on a set of facts practically identical with those here. The lessee's receiver rejected the lease and returned the keys to the landlord, who received them without objection and then altered and rerented the premises without consulting the receiver or the lessee. The court refused to allow the landlord's claim for rent accruing after the reentry, on the ground that the lease had been terminated by a surrender. In this respect it stated (at p. 927):

> "There has been no surrender in writing of the term as required by the statute of frauds (2 C. S. 1910, p. 2610, § 2), and if the surrender is found to have taken place, it must have arisen by act and operation of law, and the conduct of the landlord in accepting the keys without objection, and in entering upon the premises without consulting the receiver, and making changes and alterations therein that were not necessary as repairs for the preserva-

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[9] In the recent case of *Clark* v. *Byrne*, 187 Atl. 165, 167, the New Jersey Court of Errors and Appeals said of its earlier decision:

> "The doctrine of surrender by operation of law is amply reviewed and stated in *Sypherd* v. *Myers* * * *".

> tion of the building, and in advertising the premises for rent, and in renting the greater part of them for less than the balance of the demised term and for less than the annual rent fixed by the lease, without authority from the receiver and without consulting him, indicate an intention on the part of the landlord to accept the receiver's abandonment as a surrender and to hold possession of the premises on his own account."

The court also stressed the fact that there was no provision in the lease giving the landlord a right to reenter and relet for the tenant's account.

(C) *The petitioner's authorities are not applicable to the facts here.*

The petitioner criticizes the Circuit Court of Appeals' holding that in the present case the reentry, reletting and substantial changes in the premises made by the landlord *taken together* show that the landlord must be held to have accepted a surrender. The petitioner's position is that even if accompanied by reletting, *repairs* made by a landlord for the purpose of preserving the premises from injury do not *per se* effect a surrender of the lease. But the cases cited for this proposition have no bearing upon the situation at bar where the changes made were in the nature of *alterations.*

In *Meeker* v. *Spalsbury,* 66 N. J. L. 60, the lease provided that the landlord might enter *at any time* in order to make repairs necessary for the preservation of the premises, and also that the landlord might relet for the account of the tenant. Upon abandonment by the tenant the landlord made alterations, and, since the lease gave the landlord a

right to repair and not to alter, it was held that the making of alterations was inconsistent with a continuance of the landlord-tenant relation and that a surrender occurred. In the instant case there was no provision for reletting on the part of the landlord, who likewise breached a provision of the lease in making alterations before the normal expiration or other determination of the lease.

In *Banks v. Berliner,* 95 N. J. L. 267, upon abandonment by the tenant the landlord went no further than in making certain necessary repairs to the plumbing, and no question of restoring alterations arose. In *Block* v. *Bell,* 111 N. J. Eq. 551, the lease contained an express provision that if a receiver was appointed the tenant would immediately restore the premises to their condition at the commencement of the term. Consequently, on appointment of a receiver for the tenant and failure to restore, the landlord recovered a claim for the cost of the "substantial structural changes" necessary to restore the premises. In *Liskovsky* v. *Blau,* 176 Atl. 562, the record on appeal reveals that the lease expressly authorized the landlord to reenter and relet the premises as agent of the tenant and to hold the tenant liable for any deficiency (State of Case, p. 43). There was no clause, as here, in respect of alterations and improvements, and the nature of the repairs made is not disclosed, the opinion merely stating that the "proofs showed that the repairs were made for the purpose of preserving the buildings * * *" (176 Atl. at 563).

Thus, the *Liskovsky* and *Banks* cases had merely to do with necessary and apparently minor *repairs,* not *alterations,* and the *Meeker* and *Block* cases turn on the operation of express lease provisions with regard to alterations. None of the cases support a conclusion that alterations made

by a landlord, in addition to a reletting not authorized by the lease, do not effect a surrender.

The petitioner also cites *Zabriskie* v. *Sullivan,* 80 N. J. L. 673, aff'd 82 N. J. L. 545, for the proposition that repairs equivalent to restoration, even when accompanied by reletting, do not effect a surrender. The landlord in that case acquiesced in his tenant's abandonment only under protest, expressly notifying the tenant to that effect and stating that he reentered solely for the purpose of reletting for the account of the tenant. The landlord then made certain repairs which normally it would have been the duty of the tenant to make. Further, there is nothing in the case to indicate that such repairs amounted to restoration of alterations.

It is the Trustee's contention that in New Jersey, as in other jurisdictions, reentry, reletting and substantial changes in the premises for the purpose of restoration by the landlord, taken together, effect a surrender by operation of law where, as here, the lease did not empower the landlord to relet for the tenant's benefit. But the facts of the present case go even further. The lease provides that the lessor consents to the making of "alterations and/or improvements" by the lessee, "said improvements to belong to and become the property of the lessor *at the expiration or other determination of this lease*" (R. 28). Thus, by wiping out the changes made by the Debtor and restoring the premises to their original condition, the landlord clearly evidenced her understanding that the relation of landlord and tenant was at an end. See *Meeker* v. *Spalsbury, supra.*[10]

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[10]The petitioner objects to this conclusion on the ground that only improvements and not alterations were to become the property of the landlord when the lease determined. It

III

IT WAS NOT REVERSIBLE ERROR FOR THE SPECIAL MASTER TO INCLUDE IN HIS REPORT A FINDING THAT THE LANDLORD HAD RESTORED ALTERATIONS MADE TO THE LEASED PREMISES BY THE DEBTOR.

The District Court held, and was affirmed by the Circuit Court of Appeals, following the Special Master, that "the reentry of the landlord under the lease and her *subsequent* acts terminated all liability on the part of the tenant" (R. 50). The "subsequent acts" were (a) the restoration of the alterations made by the Debtor, which under the lease the landlord was only free to do at its "expiration or other determination" (R. 28), and (b) the reletting to other tenants without notice to the Debtor. The petitioner's grievance is that of these three acts (*i.e.*, the reentry, the restoration and the reletting) only the first and third were referred to in the stipulation of facts entered into by the parties, the facts with regard to the restoration being judicially noticed by the Special Master when he came to prepare his report to the District Court.

This was not made the subject of an exception to the Special Master's report (R. 43-45), nor was it assigned as error to the Circuit Court of Appeals (R. 58-61).

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seems hardly necessary to say that a provision that alterations as well as improvements were to become the landlord's property would have been surplusage. Improvements such as a shop window might conceivably be removed by the tenant, but ordinarily it would not be necessary to provide against the removal by the tenant of an *alteration* to the premises.

There had previously been filed with the Special Master (then sitting as Referee in Bankruptcy) a proof of claim on behalf of this same landlord for expenditures incurred in making the restorations in question. That proof of claim expressly stated that "the lease is now *expired* by reason of the bankruptcy." Since that proof of claim was by a general order of the District Court pursuant to Section 77B(c)(6), made part of the Court records in these proceedings, the Special Master very properly took notice of the allegations made by the landlord therein.

While not denying that the restoration actually took place nor challenging the Special Master's right to take notice thereof, the petitioner contends that it was improper for such facts to be taken into consideration by the Court below in reaching its decision. The only ground for the petitioner's complaint seems to be that in objecting to its claim on the ground that there had been a surrender of the lease, thereby terminating all future obligations of the Debtor thereunder, the Trustee only made specific reference to two of the three evidentiary facts that were the basis of the Special Master's decision, that is, to the reentry and the reletting but not to the restoration (R. 14).

The Circuit Court of Appeals was not impressed with this rather technical objection and declined to send the case back in order for the Trustee to plead a fact as to which there was no dispute. We submit that this did not constitute reversible error or grounds for the granting of a writ by this Court, particularly in the light of Rule XLVII of the General Orders in Bankruptcy promulgated by this Court which directs that the reports of special masters in proceedings under Section 77B "shall be deemed presumptively correct" and provides for the modification or rejection

of such reports only when the court is *"fully satisfied* that error has been committed".

Neither of the cases cited by the petitioner in this connection is in point. In *General Utilities Co.* v. *Helvering,* 296 U. S. 200, the Commissioner of Internal Revenue had raised a question of fact before the Circuit Court of Appeals that had not been presented to or ruled on by the Board of Tax Appeals, although the Court was without power in such a case to make any findings of fact. But in the present case the landlord's conduct in making the restoration was specifically included in the findings of fact of the Special Master, on the basis of which the Court below rendered its decision. Moreover, the petitioner, in its exceptions to the Special Master's report, did not assign as error the inclusion in the report of the facts as to the restoration.

In *Liberty National Bank* v. *Bear,* 265 U. S. 365, the case was remanded because the trustee in bankruptcy, in seeking to invalidate a lien under Section 67f of the Bankruptcy Act, had failed to allege or prove that the debtor was insolvent when the lien was obtained. There is nothing, however, to indicate that this Court would have reached the same conclusion had the Debtor's insolvency been shown by the record (even though not pleaded by the trustee), as is the case here with respect to the restoration of the alterations.

CONCLUSION

We respectfully submit that the judgment of the Circuit Court of Appeals should be affirmed.

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APPENDIX

Statute Involved

"The term 'creditors' shall include for all purposes of this section and of the reorganization plan, its acceptance and confirmation, all holders of claims of whatever character against the debtor or its property, including claims under executory contracts, whether or not such claims would otherwise constitute provable claims under this Act. The term 'claims' includes debts, securities, other than stock, liens, or other interests of whatever character. For all purposes of this section unsecured claims which would have been entitled to priority over existing mortgages if a receiver in equity of the property of the debtor had been appointed by a Federal court on the day of the approval of the petition or answer under this section, shall be entitled to such priority, and the holders of such claims, and of other claims, if any, of equal rank, shall be treated as a separate class of creditors. In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity, in a proceeding pending prior to the institution of a proceeding under this section any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor. The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which

would be provable under section 63 (a) of this Act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or reentry: * * *." (Bankruptcy Act of July 1, 1898, as amended, Section 77B (b) (10); 11 U. S. C. A. Sec. 207 (b) (10).)

DEC 14 193
CHARLES ELMORE CR
CLE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. 260.

IN THE MATTER

OF

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

CITY BANK FARMERS TRUST COMPANY, assignee of FLORENCE H. BUGBEE,
Petitioner,

against

IRVING TRUST COMPANY, as trustee of the estate of the above-named Debtor, et al.,
Respondents.

BRIEF ON BEHALF OF RESPONDENT, PREFERRED STOCKHOLDERS PROTECTIVE COMMITTEE.

SANFORD H. E. FREUND,
WINTHROP H. KELLOGG,
DOUGLAS B. STEIMLE,
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AND
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Attorneys for Preferred Stockholders Protective Committee, Respondent herein.

The Hecla Press, 225 Varick Street, N. Y. C. Tel. WAlker 5-1480.

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BRIEF ON BEHALF OF RESPONDENT, PREFERRED STOCKHOLDERS PROTECTIVE COMMITTEE.

Opinions Below.

The opinion below is reported in 83 F. (2d) 209. The District Court's opinion appears in the record at page 49; the Special Master's opinion appears in the record at page 37.

Statement of the Case.

The facts are as follows: On August 29, 1932, the Debtor was adjudged a bankrupt. It was then the lessee of premises in Trenton, New Jersey, under a lease from Mrs. Florence H. Bugbee, the Petitioner's assignor. The premises were occupied by several sub-tenants of the Debtor (R. 20). On November 15, 1932, following notice from the Debtor's trustee in bankruptcy that it would not assume the lease, Mrs. Bugbee re-entered the premises, made a lease of a portion of the premises to a new tenant, relet other portions of the premises to persons who had been, till that time, sub-tenants of the Debtor, and subsequently made other leases (R. 33-35). The acts of the landlord upon and following reentry, the courts below have held, evidenced her acceptance of surrender of the lease and termination of the Debtor's liability thereunder (R. 42, 50, 73).

On June 9, 1934, the Debtor instituted the present proceedings by filing its petition under Section 77-B of the Bankruptcy Act. Petitioner thereupon filed a claim alleging damages for the rejection of the lease in 1932.

The Special Master, the District Court and the Circuit Court have held that the Petitioner has no standing as a creditor in these proceedings. The Petitioner appeals from the disallowance of its claim.

The Statute.

Section 77-B, subdivision (b) (10), of the Bankruptcy Act, so far as material, reads as follows:

> "The term 'creditors' shall include for all purposes of this section and of the reorganization plan, its acceptance and confirmation, all holders of claims of whatever character against the debtor or its property, including claims under executory contracts whether or not such claims would otherwise constitute provable claims under this Act. * * *
>
> "In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this

section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity, in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor. The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63 (a) of this Act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of re-entry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or re-entry."

Summary of Argument.

This brief will be confined to answering the principal point urged by Petitioner, to wit, that its assignor has a valid claim, under such statute, for injury arising from "rejection" of the lease by the Debtor's trustee in bankruptcy, notwithstanding that she may have terminated the Debtor's liability following such rejection and long before the statute was enacted.

I.

Section 77-B makes no provision for the allowance of claims based on rejection of leases under which the debtor's liability had ceased prior to the enactment of the statute.

The history and language of the statute do not, we submit, disclose a purpose upon the part of Congress to confer a creditor status upon anyone who has released his claim against the debtor or otherwise terminated the debtor's liability to him.

It is clear from an examination of the Congressional debates and committee reports that it was the intention of Congress to recognize, for the purposes of a reorganization under the Act, certain actual legal claims which had not been previously "provable" in bankruptcy because they were contingent claims or had not come into existence at the time of the bankruptcy adjudication. The principal purpose of the legislation was to provide an instrumentality for speedy reorganization of financially embarrassed corporations and to prevent unreasonable minorities from blocking fair and equitable plans of reorganization. To accomplish the desired purpose Congress extended the doctrine of composition provided for in Section 12 of the Bankruptcy Act passed in 1898. *Downtown Inv. Assn.* v. *Boston Met. Bldgs., Inc.*, (C. C. A. 1) 81 F. (2d) 314.

None of the bills introduced to provide for the reorganization of private corporations preceding H. R. 5884, which became Sections 77-A and 77-B, except H. R. 5009, throw any special light upon the matter. They indicate no purpose, however, to recognize as creditors persons who are not creditors.

H. R. 5884, as passed by the House, contained the following provisions [Sec. 79 (b) (10)]:

> "* * * The term 'creditors' shall include for all purposes of this section and of the reorganization plan, its acceptance and confirmation, all holders of claims of whatever character against the debtor or its property, including claims under executory contracts and for future rent, whether or not such claims would otherwise constitute provable claims under this Act.
>
> "In case any executory contract shall be rejected, the same shall be deemed to have been breached and the holder shall be entitled to file a claim for damages for such breach and such claim may be allowed provided such contract shall not have been terminated by forfeiture, re-entry or otherwise."

H. R. 5009 contained similar provisions.

After H. R. 5884 had passed the House, and when it was before the Senate, the first clause quoted above was amended

by the omission of the words "and for future rent." This was Senate Amendment 13. And the clause with respect to the effect of rejection of executory contracts was amended to read as follows:

> "In case any executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee in bankruptcy or receiver in equity in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor to the extent of the injury resulting from such rejection: Provided, That the claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall not be treated as a claim ranking on a parity with debts which would be provable under section 63(a) of this Act, except up to any amount equal to the rent reserved by said lease for the year next succeeding the date of the order approving the petition or answer under this section plus an amount equal to the unpaid rent accrued up to said date, but the balance, if any, of such claim shall be subordinated in rank to debts so provable."

This was Senate Amendment 14. Both amendments were offered from the floor without explanation, and were adopted without debate.

Subsequently, in conference, the clause quoted above as Senate Amendment 14 was further amended to the form in which it appears in Section 77-B (House Report No. 1821, 73d Congress, 2d Session). As the reason for the amendments was not stated, we are confined to consideration of the language of the two clauses.

The statute was amplified to compensate a landlord whose lease has been rejected in a prior proceeding. But both provisions are conditional upon injury, the substituted provision, as well as the original provision, plainly implying that a claim resting on rejection shall be subject to legal defenses.

The condition attached to the original provision was imperfectly expressed as is pointed out in the brief of the Trustee. The condition expressed in the substituted provision by the word "injured" is precise if given its legal connotation.

Congress knew that the affairs of corporations that might desire to reorganize under the new statute were being administered in equity receivership proceedings in state and federal courts and in bankruptcy proceedings. Leases had been disaffirmed in many of these proceedings; and many of the landlords whose leases had been so rejected had not terminated the liability of their landlords under their leases although they had repossessed themselves of their properties. Various devices were adopted to keep alive the leases or the liability of the bankrupt tenant.* Leases disaffirmed in such a prior proceeding but kept alive would, presumably, be considered burdensome assets in a proceeding under Section 77-B. Congress, accordingly, indicated that another disaffirmance of such leases would be unnecessary in the new proceeding. It was proper that such landlords, whose rights against the Debtor would be terminated in the reorganization, as well as landlords with surviving covenants for damages or indemnity and landlords whose leases would be expressly rejected in the reorganization proceeding itself, should be treated as creditors under the new law.

The Petitioner further suggests that liability on such claims as the Petitioner's is the price to be paid by the Debtor for the benefits conferred by the Reorganization Act and its release from the old bankruptcy proceeding, and that the Debtor assumed liability for all rejections of leases in the bankruptcy proceeding by filing its petition for relief under Section 77-B. Petitioner fails to take into consideration that the reorganization proceedings might have been instituted by the Debtor's creditors, and that the creditor status of a landlord does not depend upon any distinction as to how the proceedings are instituted, or upon whether the prior proceeding was a state or federal equity receivership, or a federal bankruptcy proceeding.

---

* Concededly, the Petitioner's assignor might have kept alive the liability of the Debtor by simply notifying the Debtor that she would re-enter and re-rent for its account.

The Petitioner's argument also overlooks the consequences of the construction which it urges. Not only would the *debtor's* burdens be added to; actual creditors of the debtor would be penalized. We question whether any plan can be said to be fair and equitable and not unfairly discriminatory against any class of creditors or stockholders if that plan makes substantial provision for parties who have no claims at law or in equity against the debtor.

The Petitioner and other claimants with similar interests urge that the decision in the *Kuehner* case, 85 F. (2d) 35, is inconsistent with the determination of the Circuit Court in the instant case. We see no such inconsistency. It is our understanding that the distinction, by reason of which the claim in the *Kuehner* case was allowed, was that the claimants there were "creditors," as such word is defined in Section 77-B, and that it was the intention of Congress that compensation should be awarded for the termination of their contract right. We have no doubt but that Congress may require the liquidation of a contract right in a reorganization proceeding under Section 77-B, recognizing the right, though no action could at the time be maintained on the contract in a state or federal court. This was the situation before the Court in *Hermitage* v. *Levine*, 248 N. Y. 333. We do doubt the power of Congress, retroactively, to provide that rejection of a lease in a prior proceeding shall give rise to a liability where all liability on the lease has been terminated.

Summarized, the Petitioner's contentions are that the language of Section 77-B with respect to claims is to be interpreted without regard to the normal meanings attributed at law to the words "damages" and "injury"; and that since no defenses are mentioned in Section 77-B, no defenses should be allowed.

We submit that Section 77-B must be interpreted against the background of existing law; that the word "damages" cannot mean other than "legal damages"; that the word "injury" cannot mean other than "legal injury"; and that defenses, existing at law and in equity, should be available in reorganization proceedings, as they always have been against claims in bankruptcy.

CONCLUSION.

The order appealed from should be affirmed.

Respectfully submitted,

SANFORD H. E. FREUND,
WINTHROP H. KELLOGG,
DOUGLAS B. STEIMLE,
Counsel.

SHEARMAN & STERLING
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Respondent herein.

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Supreme Court of the United States

OCTOBER TERM, 1936.

No. 260.

IN THE MATTER
OF
UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

CITY BANK FARMERS TRUST COMPANY,
ASSIGNEE OF FLORENCE H. BUGBEE,
Petitioner,
against
IRVING TRUST COMPANY, AS TRUSTEE OF THE ESTATE OF THE ABOVE-NAMED DEBTOR, *et al.*,
Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

Motion of John Gerdes and John Godfrey Saxe for leave to file brief as Amici Curiae, and Brief of Amici Curiae.

JOHN GERDES,
JOHN GODFREY SAXE,
Amici Curiæ.

The Evening Post Job Printing Office, Inc., 80 Lafayette St., New York, N. Y.

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Supreme Court of the United States

OCTOBER TERM, 1936

IN THE MATTER OF UNITED CIGAR STORES COMPANY OF AMERICA, Debtor.	
CITY BANK FARMERS TRUST COMPANY, assignee of Florence H. Bugbee, Petitioner, AGAINST IRVING TRUST COMPANY, as Trustee of the Estate of the above-named Debtor, *et al.*, Respondents.	No. 260.

MOTION FOR LEAVE TO FILE BRIEF AS AMICI CURIAE

MAY IT PLEASE THE COURT:

The undersigned, with the consent in writing of all the parties, respectfully move for leave to file the accompanying brief as *Amici Curiæ* on behalf of Ella May Voight, Dorothy Voight, and Edward B. Lucius, as Trustees of the William F. Voight Trust, upon the application of the above Petitioner for a writ of certiorari to the United States Court of Appeals for the Second Circuit.

JOHN GERDES,
JOHN GODFREY SAXE,
Amici Curiæ.

BRIEF OF JOHN GERDES AND JOHN GODFREY SAXE, AS AMICI CURIAE

Preliminary Statement

The *Amici Curiæ* are the attorneys for Ella May Voight, Dorothy Voight and Edward B. Lucius, as Trustees of the William F. Voight Trust. The Voight Trust has a claim against the estate of the Debtor in the sum of over $200,000. The provability of this claim depends upon the question of law which is involved in this case.

All further references to facts in this brief will be to the facts of the claim of Petitioner herein and not to the facts of the claim of said Voight Trust.

The Question

This case presents the question whether in proceedings under Section 77B of the Bankruptcy Act a landlord may prove a claim for injury resulting from the rejection of his lease by the trustee in the bankruptcy proceeding in which the 77B petition was filed, where the lease contained no covenant for damages or indemnity and the applicable state law gave no claim for damages for breach of a covenant to pay rent, and where the landlord terminated the lease by reentry after the rejection and prior to the enactment of Section 77B.

If such a claim is provable, the judgment below is erroneous regardless of the correctness of the decision on the question of New Jersey law also involved in the case.

The Statute

"A plan of reorganization . . . (6) may reject contracts which are executory in whole or in part, including

unexpired leases . . ." Bankruptcy Act § 77B (b)(6), 11 U. S. C. A. § 207 (b)(6).

"The term 'creditors' shall include for all purposes of this section and of the reorganization plan, its acceptance and confirmation, all holders of claims of whatever character against the debtor or its property, including claims under executory contracts whether or not such claims would otherwise constitute provable claims under this Act.. * * *

"In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity, in a proceeding pending prior to the institution of a proceeding under this section any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor. The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63 (a) of this Act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or reentry: Provided, That the court shall scrutinize the circumstances of an assignment of future rent claims and the amount of the consideration paid for such assignment in determining the amount of damages allowed assignee hereunder" Bankruptcy Act § 77B (b)(10), 11 U. S. C. A. § 207 (b)(10).

". . . the judge, . . . (5) may direct the rejection of contracts of the debtor executory in whole or in part; . . ." Bankruptcy Act § 77B (c)(5), 11 U. S. C. A. § 207 (c)(5).

Opinion of the Circuit Court of Appeals

The opinion of the Circuit Court of Appeals in this case is reported in *In re United Cigar Stores Co. of America (City Bank Farmers Trust Co.)*, 83 F. (2d) 209. A more complete statement of the Circuit Court's views on the question involved herein is found in *In re United Cigar Stores Co. of America (Otis)*, 83 F. (2d) 202, at 206, and in *In re United Cigar Stores Co. of America (Kuhner-Fischer)*, C. C. A., Second Circuit, July 14, 1936, not yet reported.

The Circuit Court of Appeals held that a claim is not provable in proceedings under Section 77B for the injury resulting from the rejection of a lease in a prior bankruptcy proceeding unless, at the inception of the 77B proceedings, the landlord had a claim under applicable state law or under a covenant for damages or indemnity in the lease; and that there is no provable claim if the lease was terminated after the rejection without the survival of a claim under applicable state law or under a covenant for damages or indemnity.

The position of the Circuit Court is summarized in the following statement from its opinion in the *Kuhner-Fischer* case, *supra:* "we cannot suppose that Congress was trying to make over the contract by imposing a liability for future rent on the lessee after the term had ended. Indeed, we should have considerable doubt whether the bankruptcy power would support such an effort."

SUMMARY OF ARGUMENT

Point I

Section 77B eliminates the distinction between the provability of claims under leases and claims under other executory contracts.

Point II

The interpretation of the Court below makes the provision in Section 77B giving a claim for the rejection of a lease, meaningless and of no effect. Its decision on the Kuhner-Fischer claim (In re United Cigar Stores Co. of America (Kuhner-Fischer), C. C. A. Second Circuit, July 14, 1936, not yet reported) is contradictory to its decision in the case at bar.

Point III

The language of Section 77B is similar to that used in the English Bankruptcy Acts and should be given the same meaning.

Point IV

Surrender or reentry, after rejection of the lease, does not deprive the landlord of his claim. On the contrary, it is a condition precedent to proof of the injury resulting from such rejection.

Point V

Section 77B gives a provable claim where the lease was rejected and terminated prior to the enactment of Section 77B in a bankruptcy proceeding which is still pending when the proceedings under Section 77B are initiated.

Point VI

The grant of a provable claim for the injury caused by the rejection of a lease in a bankruptcy proceeding pending when Section 77B was enacted is not unconstitutional.

POINT I

Section 77B eliminates the distinction between the provability of claims under leases and claims under other executory contracts.

Prior to the amendment of Section 63(a) of the Bankruptcy Act and the enactment of Section 77B of the Bankruptcy Act, in June, 1934, the courts refused to give the same provable claim for the breach of an executory lease contract as was given for the breach of other executory contracts.

The injustices caused by this discrimination are well illustrated in the case at bar. The landlord had a contract of lease under which she was entitled to substantial sums of money for the use of her property for a period which was not to terminate until 1946. The lessee was adjudicated bankrupt. Until the intervention of bankruptcy the lease remained in full force and effect and neither party had violated any of its covenants. After the adjudication in bankruptcy the terms of the lease were not performed by the bankrupt, nor were they assumed or performed by its receiver or trustee in bankruptcy.

Creditors having claims for injury resulting from the rejection of executory contracts other than leases were given the right to participate, for the injury resulting from the abrogation of their contracts, in the division of the bankrupt's assets. This landlord, injured by the rejection of her executory lease contract, had no provable claim. It is true that she could have kept the lease alive, in spite of the fact that it was not being performed, and could have held the bankrupt (shorn of all its assets) for the performance of the lease; but this was a "paper" right which had no value, since the bankrupt had been deprived of all power to perform the lease.

If Section 77B does not grant provable claims to landlords for leases rejected in proceedings under the Section,

greater injustices will result than formerly resulted in bankruptcy. Bankruptcy proceedings discharge only *provable* debts. Proceedings under Section 77B discharge all debts and liabilities, regardless of their provability. Bankruptcy Act § 77B(g), (h).

Except for the limitation on the amount for which a rent claim may be proved, the provisions in Section 77B regarding executory contracts and unexpired leases are identical. See clause (6) and text following clause (10) of subdivision (b), and clause (5) of subdivision (c).

The *Amici Curiæ* respectfullly urge that Section 77B eliminates the distinction between the provability of claims under leases and claims under other executory contracts, and makes the doctrine of *Central Trust Co.* v. *Chicago Auditorium*, 240 U. S. 581, applicable to leases of real estate.

Under Section 77B, as under the doctrine of the foregoing case, the claim is given for the injury resulting from the rejection of the contract or lease (failure to adopt or assume it) by the receiver or trustee of the estate in liquidation or reorganization. It is given for the breach of an "implied term of every contract that the promisor will not permit himself, through insolvency or acts of bankruptcy, to be disabled from making performance . . ." (240 U. S. 581, 591).

The rejection is not a *breach* of the contract or lease. The breach antedates the "rejection" (failure of the receiver or trustee to assume), and occurs when the lessee or contractor permits itself to be deprived of the power of performing its obligations by surrender of all its assets to the bankruptcy court and its receiver or trustee. This breach occurs upon the initiation of the proceedings and not when the receiver or trustee fails to assume or adopt the contract or lease.

After his appointment, the receiver or trustee has a reasonable period of time within which to adopt or assume

the contract or lease. If he assumes or adopts within such period, the court, as a court of equity, will not (in the absence of an express covenant) permit a forfeiture of the contract or lease because of the prior breach.

The receiver or trustee is under no obligation to assume or adopt the contract or lease. His failure to do so ("rejection") is therefore not a breach.

Except for a limitation in the total amount which may be proved, Section 77B measures the claim for a rejection of a lease just as in the case of any other executory contract. In the absence of an express provision in the contract, it liquidates the claim by discounting future rent payments due under the contract and subtracting the appraised value of the use of the premises for the balance of the term. If the lease has a covenant for damages or indemnity—if the parties have expressly agreed upon the measure of the claim—and the measure is not too speculative to admit of reasonable proof and is not in the nature of a penalty—the claim is measured by the terms of the covenant for damages or indemnity. If the covenant for damages or indemnity is in the nature of a penalty or is too speculative to admit of reasonable proof, the covenant must be disregarded and the claim measured as though the lease contained no covenant for damages or indemnity.

Until the landlord is given the right to possession of the premises by "surrender" by the receiver or trustee, or until the landlord takes possession through "reentry", he is entitled to all accrued and unpaid rent; thereafter (since he has possession of the premises or may take such possession) he is entitled to prove a claim only for the difference between the reasonable value of the use of the premises and the rent reserved in the lease, limited however to a sum amounting to not more than three years of rent.

Complete and equitable relief is thus given to landlord and tenant. The tenant is relieved of future obligations under the lease. The landlord is given a provable claim against the estate of his lessee.

POINT II

The interpretation of the court below makes the provision in Section 77B giving a claim for the rejection of a lease, meaningless and of no effect. Its decision on the Kuhner-Fischer claim is contradictory to its decision in the case at bar. (In re United Cigar Stores Co. of America (Kuhner-Fischer), C. C. A. Second Circuit, July 14, 1936, not yet reported).

The theory of the Circuit Court of Appeals, that no claim is provable unless the lessor has a claim under applicable state law or under a covenant for damages or indemnity when the 77B proceedings are initiated, ignores the fundamental basis of the claim given to the landlord by Section 77B. It erroneously fails to base the claim upon a *rejection* of the lease, or even upon the lease itself; it bases the claim upon a debt created by a prior breach of the lease, or upon a new contract for damages or indemnity arising upon the termination of the lease (*Manhattan Properties* v. *Irving Trust Co.*, 291 U. S. 320, 338).

If this erroneous theory is applied, the grant of a claim when the lease "shall have been rejected by a trustee . . . in bankruptcy . . . in a proceeding under this section" [Bankruptcy Act § 77B (b) (10)] is redundant and wholly without meaning, for it is obvious that even without such provision all debts and contract claims which are valid and enforcible against the debtor when the petition under Section 77B is filed are provable in the proceedings.

The language of Section 77B which gives a claim for the injury sustained by a lease rejection is unnecessary and useless if its only effect is "to make some valid claims provable in proceedings under Section 77B which were not before provable in bankruptcy" (Opinion below, in this case, 83 F. (2d) 209, 211). Section 77B elsewhere

makes existing claims "provable" regardless of whether they would have been provable in ordinary bankruptcy proceedings. Subdivision (b) (10) provides that the term "creditors" shall include "holders of claims of whatever character against the debtor or its property, including claims under executory contracts, *whether or not such claims would otherwise constitute provable claims under this Act*" (Italics ours).

The Circuit Court of Appeals has recently rendered a decision which is inconsistent with its decision in the case at bar. In *In re United Cigar Stores Co. of America* (*Kuhner-Fischer*), C. C. A. Second Circuit, July 14, 1936, not yet reported, the Court allowed a claim under a covenant of indemnity although under the applicable state and federal decisions the claim is too speculative to be proved.

In the *Kuhner-Fischer* case, as in this case, the trustee in the prior bankruptcy proceeding rejected the lease. In each case the landlord reentered after such rejection. In the *Kuhner-Fischer* case the lease contained a covenant of indemnity under which it was agreed that if the lessee should be adjudicated a bankrupt the landlord might reenter and the lessee would then "indemnify the landlord against all loss of rent which the landlord may incur by reason of such termination during the residue of the term". In the case at bar the lease contained no such covenant. The Circuit Court of Appeals allowed the claim in the *Kuhner-Fischer* case but denied the claim in the case at bar.

In the *Kuhner-Fischer* case, the Court correctly held that an absolute liability of the lessee on the covenant of indemnity was created by the bankruptcy of the lessee and the reentry of the landlord, and that such liability still existed when the proceedings under Section 77B were initiated. However, instead of allowing a claim on the liability created by this covenant, the Court allowed the claim as for an injury resulting from the rejection of the lease in bankruptcy.

In the *Kuhner-Fischer* case the landlord had no "claim against a lessee for damages or indemnity under a covenant contained in a lease which would have been recoverable in a civil action had there been no 77B petition approved . . ." (*In re United Cigar Stores Co. of America (Otis)*, 83 F. (2d) 202, 206). The amount of the claim on the new contract of indemnity was too speculative to be proved or recovered under applicable state law until the end of the original term of the lease (*Hermitage Co.* v. *Levine,* 248 N. Y. 333).

In addition, the claim actually allowed was different from, and contradictory to, the claim given to the landlord by the express language of the covenant. Under the contract of indemnity, the claim was to be measured by the difference, at the end of the term of the lease, between the amounts of rent actually collected by the landlord during the term and the total rents to be paid under the lease. The Court permitted "the claim to be liquidated like a claim for breach of an executory contract for chattels; that is, by discounting the future payments and subtracting the appraised value of the term from their sum".

In spite of its statement that "we cannot suppose that Congress was trying to make over the contract", the Court actually *did* make over the contract of indemnity by allowing a claim which was not based on such contract of indemnity. As this Court stated in *Manhattan Properties* v. *Irving Trust,* 291 U. S. 320 at page 337:

> "These [indemnity covenants] do not provide for liquidation of damages (compare *Wm. Filene's Sons Co.* v. *Weed, supra*), nor indeed for any right to damages for breach of the covenant to pay rent."

The result reached by the Court in determining the Kuhner-Fischer claim was sound. The claim was properly liquidated "like a claim for breach of an executory contract for chattels". But this conclusion is warranted only

on the theory that Section 77B gives the same provable claim on an executory lease as on any other executory contract; that the damages resulting from the breach of the covenant of indemnity in the Kuhner-Fischer lease were too speculative to admit of reasonable proof; and that the claim was therefore measured as though the lease contained no covenant for damages or indemnity.

On this theory, petitioner in the case at bar was entitled to the allowance of its claim.

POINT III

The language of Section 77B is similar to that used in the English Bankruptcy Acts and should be given the same meaning.

The phrase "any person injured by such rejection" is "deemed to be a creditor" closely resembles the language employed by Section 23 of the English Bankruptcy Act of 1869 (32 and 33 Vict., c. 71). After providing for the "disclaimer" of leases, that Act stated:

> "Any person injured by the operation of this section shall be deemed a creditor of the bankrupt to the extent of such injury, and may accordingly prove the same as a debt under the bankruptcy."

Prior to the enactment of this provision, claims for the injury sustained by a landlord because of a rejection of his lease in bankruptcy proceedings, where the lease contained no covenant for damages or indemnity, were not provable. This language in the English Bankruptcy Act of 1869 served to make such claims provable.

> "In England such claims were not provable under the Act of 7 Geo. I, c. 31; *Mayor* v. *Steward,* 4 Burr. 2439; and a discharge could not be pleaded in defense of an action for rent accruing subsequent to bankruptcy. *Boot* v. *Wilson,* 8 East 311. The landlord's claim for loss of future rent was made provable by

the Act of 32 and 33 Vict., c. 71, § 23 (1869), and more explicit provisions to the same effect were embodied in that of 46 and 47 Vict., c. 52, §§ 37 and 55 (1883)."

Manhattan Properties v. Irving Trust Co., 291 U. S. 320, 332.

Substantially the same language as was used in the English Bankruptcy Act of 1869 was repeated in the English Bankruptcy Act of 1883 (46 and 47 Vict., c. 52, Sec. 55). Again, the similarity to Section 77B is apparent:

"(7) Any person injured by the operation of a disclaimer under this section shall be deemed to be a creditor of the bankrupt to the extent of the injury and may accordingly prove the same as a debt under the bankruptcy."

The law as fixed by the foregoing section has been stated by an English authority to be as follows:

"8. *Proof for injury done by the disclaimer.*—By sub-section (7) of Section 55 any person injured by the operation of a disclaimer is to be deemed a creditor of the bankrupt to the extent of the injury, and may accordingly prove the same as a debt under the bankruptcy. The measure of the damages, so far as the rent is concerned, will be the difference between the rent due under the lease for the residue of the term and the rent now to be obtained (Re Llynvi Coal Co., 7 Ch. 28), and it will include also the sum required to leave the property in the same state as if the covenants had been properly performed."

Disclaimer of Leasehold Property in Bankruptcy, 42 Solicitors' Journal 228, 230 (1898).

POINT IV

Surrender or reentry, after rejection of the lease, does not deprive the landlord of his claim. On the contrary, it is a condition precedent to proof of the injury resulting from such rejection.

Section 77B (b) provides that the claim of a landlord resulting from the rejection of an unexpired lease shall be: (1) for all "unpaid rent accrued up to such *date of surrender or reentry*"; plus (2) "an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the *date of surrender* of the premises to the landlord or the *date of reentry* of the landlord, whichever first occurs * * *." (Italics ours.)

It is evident, therefore, that no claim is provable until after there has been either a "surrender of the premises to the landlord" or a "reentry of the landlord".

Surrender or reentry by the landlord not only does not take away the claim given by Section 77B, but it is a condition precedent to the provability of such a claim, for without a surrender or reentry there is no prescribed method for fixing the amount of the claim.

Even aside from the express provision in Section 77B, it is obvious that the landlord's claim may reasonably be measured only if the lease is terminated. An obligation to pay rent remains against the tenant so long as the lease is alive. While this liability exists, the amount of the damage which the landlord will sustain will be contingent upon the extent to which rent is paid in the future by the tenant or his assignee. If this possibility of performance is not eliminated, the damage which the landlord will sustain will be too speculative to permit of reasonable ascertainment.

One of the reasons given by the Courts for not allowing rent claims in bankruptcy proceedings, prior to the amend-

ment of Section 63 a of the Bankruptcy Act in 1934, was "because of the uncertainty at the date of adjudication that the lessor will reenter" (*Manhattan Properties* v. *Irving Trust*, 291 U. S. 320, 331).

The original rent provision in the Bill which enacted Section 77B (H. R. 5884, 73rd Cong. 1st Sess.) declared that a claim under a rejected executory contract would be allowed "provided such contract shall not have been terminated by forfeiture, reentry or otherwise." The omission of this language in the Act as passed, must be taken as a clear indication of a change in the intent of Congress.

POINT V

Section 77B gives a provable claim where the lease was rejected and terminated prior to the enactment of Section 77B in a bankruptcy proceeding which is still pending when the proceedings under Section 77B are initiated.

The recent decision of the Circuit Court of Appeals in proceedings involving this Debtor (*In re United Cigar Stores Co. of America* (*Kuhner-Fischer*), C. C. A. Second Circuit, July 14, 1936, not yet reported), allowed a claim for the rejection of a lease in a prior bankruptcy proceeding where such rejection occurred and the lease was terminated prior to the enactment of Section 77B.

Section 77B (b) gives the landlord a claim for the resultant injury "in case an * * * unexpired lease of real estate * * * shall have been rejected by a trustee or receiver in *bankruptcy* * * * *in a proceeding pending prior to the institution of a proceeding under this section* * * *." It also provides that the limitation of the landlord's claim shall be measured from "the date of the surrender of the premises to the landlord or the

date of reentry of the landlord, * * * *whether before or after the filing of the petition* * * *"* (Italics ours.).

This language is so clear that no argument seems necessary to establish the intent of Congress to bestow upon the landlord a claim for injury caused by the rejection of his lease in a prior bankruptcy proceeding, even if the premises were surrendered to the landlord, or he reentered, "*before* * * * the filing of the petition * * *" initiating the proceedings under Section 77B (Italics ours).

Section 77B also provides:

> "(p) This section shall take effect and be in force from and after the date of the approval of this amendatory Act and *shall apply* as *fully to debtors*, their stockholders *and creditors, whose interests or debts have been acquired or incurred prior to such date*, as to debtors, their stockholders and creditors, whose interests or debts are acquired or incurred after such date. *Proceedings under this section may be taken in proceedings in bankruptcy which are pending on the effective date of this amendatory Act*" (Italics ours.).

A consideration of the conditions which existed at the time when Section 77B was enacted makes it manifest that Congress intended to give relief to landlords who had been unjustly deprived of their rights by the rejection of leases in bankruptcy proceedings prior to the enactment of Section 77B.

The Debtor and other chain store corporations with numerous executory leases had voluntarily instituted bankruptcy proceedings in 1932. Although bankruptcy proceedings are usually intended for liquidation rather than reorganization, and these corporations desired reorganization, they went into bankruptcy because it afforded them an opportunity to avoid more lease claims than in an equity receivership.

On August 29, 1932, the order adjudicating the Debtor a bankrupt was entered. Within less than three months all its burdensome leases had been rejected.

The use of bankruptcy proceedings merely to cut off the claims of landlords was generally criticized, and almost became a national scandal. The facts were well known to the members of Congress. It was natural therefore for Congress to provide in Section 77B that a corporation desiring to discontinue pending bankruptcy proceedings and avail itself of the benefits of reorganization under Section 77B, could do so only if it granted the landlord a provable claim for the injury which he had previously sustained by the rejection of his lease in bankruptcy.

Section 77B was enacted on June 7, 1934. Within two days the Debtor voluntarily filed its petition under the Section.

That the provision in Section 77B relating to a rejection of an unexpired lease in a prior proceeding was included with specific reference to rejections which had occurred prior to the enactment of Section 77B becomes further apparent when it is realized that in the future the spectacle of a corporation first being subjected to bankruptcy proceedings and then having its administration transferred to proceedings under Section 77B is bound to be rare. The more likely procedure will be to attempt rehabilitation of the corporation under Section 77B first and to resort to liquidation only when the futility of reorganization becomes evident. It seems therefore that corporations in bankruptcy when Section 77B was enacted were the particular debtors against whom these rent provisions were directed.

POINT VI

The grant of a provable claim for the injury caused by the rejection of a lease in a bankruptcy proceeding pending when Section 77B was enacted is not unconstitutional.

This Court has already stated that Congress may grant a provable claim for future rents under a lease which has no covenant for damages or indemnity.

> "The issue is not one of power, for plainly Congress may permit such claims or exclude them."
>
> *Manhattan Properties* v. *Irving Trust*, 291 U. S. 320, 332.

Section 77B regulates the distribution of the assets of a debtor in the possession of the bankruptcy court. It does not redefine or change the substantive law of landlord and tenant.

The proceeding initiated by this Debtor under Section 77B is merely a continuance of the prior bankruptcy proceeding in which the petition initiating the 77B proceeding was filed and in which this landlord's lease was rejected. The proceeding under Section 77B is "an amplification or new end product of the original bankruptcy, just as though the bankrupt or alleged bankrupt had proposed a composition" (*In re Paramount Publix Corp.; Greenberg* v. *Paramount Pictures, Inc.*, C. C. A., Second Circuit, July 20, 1936, not yet reported).

No constitutional rights of a debtor, or of any of its creditors or stockholders, are invaded by granting the landlord a right to prove a claim for the damages sustained by him as a result of the rejection of his lease in bankruptcy proceedings which were pending when Section 77B was enacted and when the proceedings under Section 77B were initiated.

Since creditors who extended credit after the filing of the petition in bankruptcy enjoy the priority which attaches to all expenses of administration and will therefore be paid in full before any distribution is made to the landlord, such creditors can not be injured by the allowance of the landlord's claim.

The creditors with whom the landlord is permitted to participate on a parity in the distribution of the debtor's assets under Section 77B extended credit before the filing of the petition in bankruptcy and therefore at a time when the landlord's lease was a valid and subsisting obligation of the debtor. Such creditors can not claim that assurances upon which they relied in extending credit have been defeated. As the Court said *In re Inland Dredging Corporation*, 61 F. (2d) 765, 766, "All that was done was to provide for a new division of any pot, which should in the future arise through the sequestration of the debtor's assets in bankruptcy, or any other insolvency proceedings".

In Section 64 of the Bankruptcy Act of 1898 (11 U. S. C. A. § 104), and in all prior bankruptcy Acts, Congress provided certain priorities in the distribution of bankrupt estates. As a result, creditors who have equal rights under applicable state law are relegated to a subordinate position. Frequently, some are paid in full while others receive nothing. They are thus deprived of substantial rights. But since the deprivation is incidental to an exercise of the power over bankrupt estates, there has been no violation of their constitutional rights.

Priorities given under an existing bankruptcy statute may be changed by a subsequent statute, and such a change is effective even as to claims arising prior to the change. *In re Inland Dredging Corporation*, 61 F. (2d) 765; *City of Chelsea* v. *Dolan*, 24 F. (2d) 522.

It seems clear that Congress may permit a landlord, who had a valid and subsisting contract with the Debtor when the court took custody of its assets, to participate with other creditors in the division of such assets for the injury sustained by him through the deprivation of his right to look to the Debtor's assets for the satisfaction of his claims under the lease.

The Debtor had no constitutional right to the use of Section 77B. Congress could have provided that the new procedure be available only to corporations not already in bankruptcy. When it conditioned the use of this procedure upon a recognition of landlords' claims for injuries inflicted in the bankruptcy proceedings, Congress was well within its constitutional power.

If the rights and remedies of all of the parties are actually fixed and crystallized by the bankruptcy proceeding, and such rights and remedies are only those which existed immediately prior to the filing of the petition undr Section 77B, then the use of proceedings under Section 77B by this Debtor is improper and illegal, and any creditor may insist on his right to have the assets of the Debtor liquidated as in bankruptcy in order that he may obtain the cash dividend which he would receive if the bankruptcy proceedings were consummated.

Respectfully submitted,

JOHN GERDES,
JOHN GODFREY SAXE.

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Supreme Court of the United States

OCTOBER TERM, 1936.

No. 260.

IN THE MATTER

OF

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor,

CITY BANK FARMERS TRUST COMPANY,
ASSIGNEE OF FLORENCE H. BUGBEE,

Petitioner,

against

IRVING TRUST COMPANY, AS TRUSTEE OF THE ESTATE OF THE ABOVE-NAMED DEBTOR, *et al.*,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

Supplemental Brief of John Gerdes and John Godfrey Saxe as Amici Curiae.

JOHN GERDES,
JOHN GODFREY SAXE,
Amici Curiæ.

The Evening Post Job Printing Office, Inc., 80 Lafayette St., New York, N. Y.

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CITY BANK FARMERS TRUST COMPANY, assignee of Florence H. Bugbee,

Petitioner,

AGAINST

IRVING TRUST COMPANY, as Trustee of the Estate of the above-named Debtor, *et al.*,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI.

SUPPLEMENTAL BRIEF OF JOHN GERDES AND JOHN GODFREY SAXE AS AMICI CURIAE

This supplemental brief is filed only to clear up any possible misunderstanding as to whether the *Voight* claim, represented by the *amici curiæ*, is affected by the decision in this case.

The statement in the briefs in opposition to the petition for writ of certiorari that the lease in the *Voight* claim

had been terminated *before* the trustee in bankruptcy had rejected the lease, is a statement of the *contention* of the trustee and not of a conceded fact. Whether the lease was terminated before the rejection is one of the litigated issues.

If this Court affirms the decision of the court below, the *Voight* claim *must* be denied. If, however, this Court reverses the lower court in this case, claimant will have an opportunity to litigate the disputed question as to whether the lease was terminated *before* or *after* the rejection by the trustee.

The *amici curia* are informed that many other claims involve the same disputed question of fact as to whether or not the rejection occurred before or after the termination of the lease. All of these claims will be absolutely barred if this Court sustains the decision of the lower court herein.

Respectfully submitted,

JOHN GERBER,
JOHN GODFREY SAXE,

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CHARLES ELMORE CROPLEY
CLERK

Supreme Court of the United States

OCTOBER TERM, 1936.

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Motion of John Gerdes and John Godfrey Saxe for leave to file brief and argue as *Amici Curiae*, and Brief of *Amici Curiae*.

JOHN GERDES,
JOHN GODFREY SAXE,
Amici Curiae.

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Supreme Court of the United States

OCTOBER TERM, 1936

IN THE MATTER OF UNITED CIGAR STORES COMPANY OF AMERICA, Debtor.	
CITY BANK FARMERS TRUST COMPANY, assignee of Florence H. Bugbee, Petitioner, AGAINST IRVING TRUST COMPANY, as Trustee of the Estate of the above-named Debtor, *et al.*, Respondents.	No. 260

MOTION FOR LEAVE TO FILE BRIEF AND TO ARGUE AS *AMICI CURIAE*

MAY IT PLEASE THE COURT:

The undersigned, with the consent in writing of all the parties, respectfully move this Honorable Court for leave to file the accompanying brief in this case and be heard on the oral argument as *Amici Curiae* on behalf of Ella May Voigt, Dorothy Voigt, and Edward B. Lucius, as Trustees of the William F. Voigt Trust.

JOHN GERDES,
JOHN GODFREY SAXE,
Amici Curiae.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1936

IN THE MATTER

OF

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

CITY BANK FARMERS TRUST COMPANY, assignee of Florence H. Bugbee,

Petitioner,

AGAINST

IRVING TRUST COMPANY, as Trustee of the Estate of the above-named Debtor, *et al.*,

Respondents.

BRIEF OF JOHN GERDES AND JOHN GODFREY SAXE, AS *AMICI CURIAE*

Preliminary Statement

The *Amici Curiae* are the attorneys for Ella May Voigt, Dorothy Voigt and Edward B. Lucius, as Trustees of the William F. Voigt Trust. The Voigt Trust has a claim against the estate of the Debtor in the sum of over $200,000. The provability of the Voigt claim depends upon the question of law which is involved in this case.

All further references to facts in this brief will be to the facts of the claim of Petitioner herein and not to the facts of the claim of the Voigt Trust.

The Question

This case presents the question whether in proceedings under Section 77B of the Bankruptcy Act a landlord may prove a claim for injury resulting from the rejection of his lease by the trustee in the bankruptcy proceeding in which the 77B petition was filed, where the lease contained no covenant for damages or indemnity and the applicable state law gave no claim for damages for breach of a covenant to pay rent, and where the landlord terminated the lease by reentry after the rejection and prior to the enactment of Section 77B.

If such a claim is provable, the judgment below is erroneous regardless of the correctness of the decision on the question of New Jersey law, which is also involved in the case.

The Statute

"The term 'creditors' shall include for all purposes of this section and of the reorganization plan, its acceptance and confirmation, all holders of claims of whatever character against the debtor or its property, including claims under executory contracts whether or not such claims would otherwise constitute provable claims under this Act. * * *

"In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor. The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate

or for damages or indemnity under a covenant contained in such lease shall be treated in parity with debts which would be provable under section 63 (a) of this Act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or reentry: Provided, That the court shall scrutinize the circumstances of an assignment of future rent claims and the amount of the consideration paid for such assignment in determining the amount of damages allowed under this paragraph hereunder." Bankruptcy Act § 77B (b)(10), 11 U. S. C. A. § 207 (b)(10).

"A plan of reorganization [may] (6) may reject contracts of the debtor which are executory in whole or in part, including unexpired leases [***]." Bankruptcy Act § 77B (b)(6), 11 U. S. C. A. § 207 (b)(6).

"[***] the judge [***] (5) may direct the rejection of contracts of the debtor executory in whole or in part; [***]." Bankruptcy Act § 77B (c)(5), 11 U. S. C. A., § 207 (c)(5).

Opinion of the Circuit Court of Appeals

The opinion of the Circuit Court of Appeals in this case is reported in *In re United Cigar Stores Co. of America (City Bank Farmers Trust Co.)*, 83 F. (2d) 209. A more complete statement of the Circuit Court's views on the question involved herein is found in *In re United Cigar Stores Co. of America (Otis)*, 83 F. (2d) 202, at 206, and in *Kuhner* v. *Irving Trust Co.*, 85 F. (2d) 35.

The Circuit Court of Appeals held that a claim is not provable in proceedings under Section 77B for the injury

SUMMARY OF ARGUMENT

POINT I

Section 77B gives a landlord whose lease is rejected a provable claim, limited in amount, even though no claim is given by state law and even though the lease contains no express covenant for damages or indemnity.

POINT II

The language of Section 77B is similar to that used in the English Bankruptcy Acts and should be given the same meaning.

POINT III

Section 77B eliminates the distinction between the provability of claims under leases and claims under other executory contracts.

POINT IV

The decision of the Court below on the Kuhner claim [*Kuhner* v. *Irving Trust Co.*; 85 F. (2d) 35] is contradictory to its decision on the claim in this case.

POINT V

Surrender or reentry after the rejection of a lease does not deprive the landlord of his right to prove a claim. On the contrary, it is a condition precedent to proof of the injury resulting from the rejection.

POINT VI

Section 77B grants the right to prove a claim where a lease was rejected and terminated prior to the enactment of Section 77B in a bankruptcy proceeding which was still pending when the proceedings under Section 77B were initiated.

POINT VII

The grant of the right to prove a claim for the injury caused by the rejection of a lease in a bankruptcy proceeding pending when Section 77B was enacted is not unconstitutional.

POINT VIII

The interpretation of the Court below makes redundant and of no effect the provisions in Section 77B granting the landlord a claim for the rejection of his lease.

POINT I.

Section 77B gives a landlord whose lease is rejected a provable claim, limited in amount, even though no claim is given by state law and even though the lease contains no express covenant for damages or indemnity.

Section 77B(b)(10) first provides that the term "creditors" shall include "holders of claims of whatever character against the debtor or its property, including claims under executory contracts *whether or not such claims would otherwise constitute provable claims under this Act*" (Italics ours).

This language does not purport to give any claim. It merely makes existing claims "provable" regardless of their provability in ordinary bankruptcy proceedings. Aside from specified exceptions, claims are not provable in ordinary bankruptcy proceedings unless they are in existence when the proceedings are initiated. *Zavelo* v. *Reeves*, 227 U. S. 625. In equity receivership proceedings, on the other hand, claims which are in existence before the expiration of the time fixed for filing claims may be proved even though they were not in existence when the receivership proceedings were initiated. *Wm. Filene's Sons Co.* v. *Weed*, 245 U. S. 597. This language in Section 77B serves to adopt the rule which has prevailed in equity receiverships.

This Court has held that in ordinary bankruptcy proceedings a claim arising out of an express covenant for damages or indemnity is not provable if it comes into existence after the bankruptcy petition is filed. *Manhattan Properties* v. *Irving Trust Co.*, 291 U. S. 320. This decision is *not* applicable to corporate reorganization proceed-

ings under Section 77B. The language quoted above adopts the equity receivership rule instead.

If Section 77B contained no other language dealing with the claims of landlords, the provability of such claims in 77B proceedings, under the language already quoted, would be exactly as held by the Circuit Court of Appeals in this case: a claim arising from the rejection of a lease would be provable by a landlord whenever a claim is given under applicable state law or under an effective covenant for damages or indemnity, regardless of whether the claim arose at or after the initiation of the proceedings.

But Section 77B contains additional language—language which clearly gives the landlord a remedy not previously recognized, even in equity receiverships.

Section 77(b)(10) provides:

> "In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor."

This language, supplementing the language previously quoted, defines a *new* remedy. "*Any* person injured by such rejection shall * * * be deemed to be a creditor". There is no language restricting the remedy to claims arising under state law or under leases containing express covenants for damages or indemnity.

That a landlord whose lease has been rejected may have a claim even though his lease contains no covenant for damages or indemnity is specifically recognized by Section 77B. The sentence which follows the sentence which has just been quoted refers to a "claim of a landlord for

injury resulting from the rejection" as well as to a claim "for damages or indemnity under a covenant." Bankruptcy Act § 77B(b)(10).

It is significant to note that in the form in which it originally passed the House of Representatives, H. R. 5884 (73rd Cong., 1st Sess., 77 Cong. Rec. 5009-5013, June 5, 1933), the Bill under which Section 77B was enacted, contained a materially different provision as to claims under rejected leases. The provision originally read as follows:

> "In case any executory contract shall be rejected, the same shall be deemed to have been breached and the holder shall be entitled to file a claim for damages for such breach and such claim may be allowed provided such contract shall not have terminated by forfeiture, reentry, or otherwise."

If the foregoing language had been retained in the statute as the only provision regarding rejected leases, no claim not previously existing would have been recognized. The only effect of such a provision would have been to grant provability to a claim which came into existence after the filing of the petition. The mere statement that a rejection shall operate as a breach is insufficient to give a claim in the case of a lease. The deficiency in the law as it existed prior to June, 1934, was not in its failure to regard the non-payment of rent as a breach of the lease, but in its failure to give a remedy for damages for such breach. If the trustee failed to adopt or perform the lease, rent was not forthcoming and a breach of the lease was effected. But the landlord's only remedy for such a breach, in the absence of an appropriate covenant or state statutory provision, was to bring actions from time to time as the rents became due. Most states had statutes permitting the landlord to oust the tenant from possession in summary proceedings, but practically no statutes gave the landlord a right to repossess the property and recover damages for future rents. It is apparent, therefore, that the provision originally inserted in H. R. 5884 gave no relief to the landlord except that it made a claim provable even though the

claim became effective after the institution of the proceedings.

The language which was finally incorporated into Section 77B is obviously intended to give the landlord a right to prove a claim not previously recognized—the right to prove a claim for the "injury resulting from the rejection" of the lease.

The grant of a provable claim to every landlord sustaining injury by a rejection of his lease was a conscious effort on the part of Congress to correct injustices resulting from the previous failure of the law to give a remedy for the damages sustained.

At the common law, a landlord had no claim for damages, except to the extent to which rent had accrued, for breach of a covenant to pay rent in the absence of a specific covenant for damages or indemnity. In a few states a claim was given by statute. Most states, including New York, had no statute on the subject, and consequently no claim could be proved in bankruptcy except for rent which had accrued at the time of the filing of the petition. Even when the lease contained an effective covenant for damages or indemnity, the claim was not provable in bankruptcy unless it had been in existence when the petition in bankruptcy was filed.

If the landlord had no provable claim, the lease was not discharged by the bankruptcy proceedings and the obligations of the lease survived against the bankrupt tenant. The tenant's trustee in bankruptcy was under no obligation to perform the covenant to pay rent or to perform any other covenant of the lease, unless he adopted the lease.

In the absence of an adoption by the trustee, the landlord had no claim against the estate of the bankrupt and no right to participate with other creditors of the bankrupt in the distribution of the bankrupt's assets. While, technically, the lease survived, it survived, in the case of a corporate tenant, against an entity which had

been deprived of all of its assets and which would no longer continue in business.

If, in the enactment of Section 77B, Congress has not granted a provable claim to a landlord for a lease rejected in proceedings under the Section, greater injustice will result in proceedings under Section 77B than formerly resulted in bankruptcy. Bankruptcy proceedings discharge only *provable* debts. Proceedings under Section 77B discharge *all* debts and liabilities, regardless of their provability. See Bankruptcy Act §77B(g),(h); *Foust* v. *Munson Steamship Lines*, U. S. Sup. Ct., Nov. 9, 1936, not yet reported.

The rent provisions in Section 77B should be liberally construed in order that the intent and purposes of the legislature may be given effect. Section 77B, enacted as part of the Bankruptcy Act of 1898, is clearly a remedial statute in purpose and provision. See Weinstein, *Corporations Amenable to Section 77B* (1935) 83 U. of Pa. L. Rev. 853, 863; Sabel, *The Corporate Reorganizations Act* (1934) 19 Minn. L. Rev. 34, 47. It has frequently been said that federal bankruptcy acts, being remedial in character, are entitled to a liberal construction.

> "It has been aptly said that 'the Bankruptcy Act is remedial and should be interpreted reasonably and according to the fair import of its terms, with a view to effect its objects and to promote justice' (Botts *v.* Hammond, 99 Fed. 916, 920, 40 C. C. A. 179 [C. C. A. 4]); and, in working out these ends, the bankruptcy courts have not indulged in technicalities wherever a liberal procedure was consistent with the substantial rights of the parties in interest; * * *"
>
> *Emerson* v. *Castor*, 236 Fed. 29, 34.

> "The national bankruptcy act establishes a uniform system, and regulates, in all their details, the relations, rights, and duties of debtor and creditor. It should be interpreted reasonably and according to a

fair import of its terms, with a view to effect its objects and to promote justice. Black, Bankr. 274; *In re* Muller, Fed. Cas. No. 9, 912; Silverman's Case, Fed. Cas. No. 12,855."

Blake, Moffitt & Towne v. *Francis-Valentine Co.*, 89 Fed. 691, 693.

POINT II

The language of Section 77B is similar to that used in the English Bankruptcy Acts and should be given the same meaning.

The phrase "any person injured by such rejection" is "deemed to be a creditor" [Bankruptcy Act § 77B(b)(10)] closely resembles the language employed by Section 23 of the English Bankruptcy Act of 1869 (32 and 33 Vict., c. 71). After providing for the "disclaimer" of leases, that Act stated (Sec. 23):

> "Any person injured by the operation of this section shall be deemed a creditor of the bankrupt to the extent of such injury, and may accordingly prove the same as a debt under the bankruptcy."

Prior to the enactment of this provision, claims for the injury sustained by a landlord because of a rejection of his lease in bankruptcy proceedings, where the lease contained no covenant for damages or indemnity, were not provable. This language in the English Bankruptcy Act of 1869 served to make such claims provable.

> "In England such claims were not provable under the Act of 7 Geo. I, c. 31; *Mayor* v. *Steward*, 4 Burr. 2439; and a discharge could not be pleaded in defense of an action for rent accruing subsequent to bankruptcy. *Boot* v. *Wilson*, 8 East 311. The landlord's claim for loss of future rent was made provable by the Act of 32 and 33 Vict., c. 71, § 23 (1869), and

more explicit provisions to the same effect were embodied in that of 46 and 47 Vict., c. 52, §§ 37 and 55 (1883)."

Manhattan Properties v. *Irving Trust Co.*, 291 U. S. 320, 332.

Substantially the same language as was used in the English Bankruptcy Act of 1869 was repeated in the English Bankruptcy Act of 1883 (46 and 47 Vict., c. 52, Sec. 55). Again, the similarity to Section 77B is apparent:

"(7) Any person injured by the operation of a disclaimer under this section shall be deemed to be a creditor of the bankrupt to the extent of the injury, and may accordingly prove the same as a debt under the bankruptcy."

The law as fixed by the foregoing section has been stated by an English authority to be as follows:

"8. *Proof for injury done by the disclaimer.*—By sub-section (7) of Section 55 any person injured by the operation of a disclaimer is to be deemed to be a creditor of the bankrupt to the extent of the injury, and may accordingly prove the same as a debt under the bankruptcy. The measure of the damages, so far as the rent is concerned, will be the difference between the rent due under the lease for the residue of the term and the rent now to be obtained (*Re. Llynvi Coal Co.*, 7 Ch. 28), and it will include also the sum required to leave the property in the same state as if the covenants had been properly performed."

Disclaimer of Leasehold Property in Bankruptcy, 42 Solicitors' Journal 228, 230 (1898)

Subsequent English Bankruptcy Acts have employed the language quoted from the Act of 1883.

The present language of Section 77B which resembles the language in the English statutes was inserted at a

joint Congressional Conference held shortly before the enactment of the Bill.

It is significant to note that this change in Section 77B was made in May, 1934, a few months after February, 1934, when this Court, in the *Manhattan Properties* opinion, called attention to the fact that the language in the English Bankruptcy Acts of 1869 and 1883 had made landlords' claims for loss of future rents provable.

The similarity of the language in Section 77B (except for the limitation in the amount of the claim) to the language used in the English Bankruptcy Acts makes it apparent that it was utilized with the deliberate intention of accomplishing the results which had been successfully obtained in England.

POINT III

Section 77B eliminates the distinction between the provability of claims under leases and claims under other executory contracts.

The injustices which existed in the relationship between a landlord and his bankrupt tenant prior to the enactment of Section 77B of the Bankruptcy Act (and the amendment of Section 63(a) of the Bankruptcy Act) in June, 1934, resulted from the refusal of the courts to give the same provable claim for the breach of an executory lease contract as was given for the breach of other executory contracts.

The inequitable situation created by this discrimination has already been indicated. Creditors having claims for injury resulting from the rejection of executory contracts other than leases were given the right to participate, for the injury resulting from the abrogation of their contracts, in the division of the bankrupt's assets. But a landlord whose executory lease contract had been rejected in bankruptcy proceedings had no provable claim

for the injury which he had sustained. It is true that he could keep the lease alive, in spite of the fact that it was not being performed, and could hold the bankrupt (shorn of all its assets) for the performance of the lease, but this was a "paper" right which had no value, since the bankrupt was deprived of all power to perform the lease.

It is not surprising that in 1934 Congress determined to correct this situation by extending to landlords the same right to prove claims as existed under other executory contracts.

Section 77B clearly indicates an intent to include leases among executory contracts and to give parties to executory contracts (including leases) equivalent rights. Except for the limitation upon the amount for which a claim may be proved, the provisions in Section 77B regarding executory contracts and unexpired leases are identical.

Clause (6) of subdivision (b) provides that a plan of reorganization "may reject contracts of the debtor which are executory in whole or in part, including unexpired leases [ ] [ ]".

Clause (10) of subdivision (b) defines "creditors" as including holders of claims under executory contracts "whether or not such claims would otherwise constitute provable claims" under the Bankruptcy Act. It also provides that a person injured by the rejection of "an executory contract or unexpired lease" shall have a provable claim.

Clause (5) of subdivision (c), which gives the judge in reorganization proceedings power to "direct the rejection of contracts of the debtor executory in whole or in part", without expressly referring to leases, clearly includes leases among "contracts". Unless leases are included among "contracts executory in whole or in part", no power is given to a judge to reject a lease, although subdivision (b) (10) gives a provable claim when an "executory contract or unexpired lease" has been "rejected pursuant to direction of the judge".

The *Amici Curiae* respectfully urge that this identical treatment of claims under leases and claims under other executory contracts was designed to eliminate the confusion which the courts had formerly drawn between such claims. The result is that the doctrine of *Central Trust Co. v. Chicago Auditorium* [240 U. S. 581] is now applicable to leases of real estate as well as to other executory contracts.

The fundamental principles which guided this Court when it decided the *Chicago Auditorium* case are expressed in the following quotations:

> "Coming to the merits: It is no longer open to question in this court that, as a rule, where a party bound by an executory contract repudiates his obligations or disables himself from performing them before the time for performance, the promisee has the option to treat the contract as ended, so far as further performance is concerned, and maintain an action at once for the damages occasioned by such anticipatory breach (p. 578).
>
> "* * * There is no doubt that the same rule must be applied where a similar repudiation or disablement occurs during performance (p. 580).
>
> "* * * The immediate effect of bankruptcy was to strip the company of its assets, and thus disable it from performing (p. 580).
>
> "* * * the same principle that entitles the promisee to continued willingness entitles him to continued ability on the part of the promisor. In short, it must be deemed an implied term of every contract that the promisor will not permit himself, through insolvency or acts of bankruptcy, to be disabled from making performance; and, in this view, bankruptcy proceedings are but the natural and legal consequence of something done or omitted to be done by the bankrupt, in violation of his engagement. It is the purpose of the Bankruptcy Act, generally speaking, to permit all creditors to share in the distribution of the assets of the bankrupt, and to leave the honest debtor thereafter free from liability upon previous obligations. *Williams* v. *U. S. Fidelity Co.*, 236 U. S. 549, 554. Executory agreements play so

> important a part in the commercial world that it would lead to most unfortunate results if, by interpreting the Act in a narrow sense, persons entitled to performance of such agreements on the part of bankrupts were excluded from participation in bankrupt estates, while the bankrupts themselves, as a necessary corollary, were left still subject to action for non-performance in the future, although without the property or credit often necessary to enable them to perform. We conclude that proceedings, whether voluntary or involuntary, resulting in an adjudication of bankruptcy, are the equivalent of an anticipatory breach of an executory agreement, within the doctrine of *Roehm* v. *Horst*, *supra*." (pp. 591-2.)

Under Section 77B, as under the doctrine of the *Chicago Auditorium* case, the claim is given for the breach of an "implied term of every contract that the promisor will not permit himself, through insolvency or acts of bankruptcy, to be disabled from making performance . . ." (240 U. S. 581, 591). This breach occurs upon the initiation of the proceedings when the lessee or contractor permits itself to be deprived of the power of performing its obligations by surrender of all its assets to the bankruptcy court or its receiver or trustee.

After his appointment, the receiver or trustee has a reasonable period of time within which to adopt or assume the contract or lease.

If he assumes or adopts the contract or lease within such period and thereafter fully performs its terms and conditions, the court, as a court of equity, will disregard (in the absence of an express covenant to the contrary) the prior "equivalent of an anticipatory breach", and will not permit a forfeiture of the contract or lease. No "injury" has resulted to the contractor or landlord. The assets of the debtor in the possession of the court are now available for the satisfaction of claims arising under the contract or lease which was assumed or adopted by the receiver or trustee.

If the contract or lease is not assumed or adopted by the receiver or trustee, the full effect of "the equivalent of an anticipatory breach" remains unmitigated. The contractor or landlord is "injured". He cannot enforce his contract or lease against the assets of his debtor or lessee.

> "As we have seen in the Termination of Lease Proceeding, a receiver is entitled to a reasonable time in which to determine whether to adopt or renounce the contracts of the corporation for which he is appointed. During this trial period the operations under the contract may go on and the legal consequences flowing from the fact of the receivership may be suspended in their operation. If the receiver elect to adopt the contract, his adoption relates back to the beginning of the receivership and the contract continues as if nothing had taken place. That which would otherwise have amounted to a breach of the contract does not have that effect on account of the receiver's acceptance of it. On the other hand, it necessarily follows that when a receiver rejects a contract, his rejection relates back to the beginning of the receivership and the breach of the contract takes place as of that time."
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> *Pennsylvania Steel Co.* v. *New York City Ry. Co.*, 198 Fed. 721, 744.

Every failure of the receiver or trustee to assume or adopt a contract or lease is a "rejection". No other sensible meaning can be given to this term as used in Section 77B. Any attempt to distinguish a mere failure to assume or adopt from an affirmative act of "rejection" would make it possible for the receiver or trustee to withhold a claim under Section 77B by inaction or to grant a claim by affirmative rejection. This, obviously, would be highly objectionable.

This view is in accord with the view of this Court in the *Chicago Auditorium* case. In that case there was no affirmative act of rejection. There was merely a failure to assume or adopt the contract.

The *rejection* is not a *breach* of the contract or lease. The receiver or trustee is under no obligation to assume or adopt the contract or lease. His failure to do so ("rejection") is therefore not a breach.

The breach antedates the "rejection" (failure of the receiver or trustee to assume), and occurs when the lessee or contractor permits itself to be deprived of the power of performing its obligations by surrender of all its assets to the bankruptcy court and its receiver or trustee. This breach occurs upon the initiation of the proceedings and not when the receiver or trustee fails to assume or adopt the contract or lease.

Under Section 77B the claim is not given for a *breach* of the lease caused by its rejection, but for the "injury resulting from the rejection". As an assumption or adoption of the lease by the receiver or trustee results in its performance, the "injury resulting from the rejection" (failure to assume or adopt) is measured by the value to the landlord of performance of the lease.

Except for a limitation in the total amount which may be proved, Section 77B measures the claim for a rejection of a lease just as in the case of any other executory contract. In the absence of an express provision in the contract, it liquidates the claim by discounting future rent payments due under the contract and subtracting the appraised value of the use of the premises for the balance of the term. If the lease has a covenant for damages or indemnity—if the parties have expressly agreed upon the measure of the claim—and the measure is not too speculative to admit of reasonable proof and is not in the nature of a penalty, the claim is measured by the terms of the covenant for damages or indemnity. If the covenant for damages or indemnity is in the nature of a penalty or is too speculative to admit of reasonable proof, the covenant must be disregarded and the claim measured as though the lease contained no covenant for damages or indemnity.

Until the landlord is given the right to possession of the premises by "surrender" by the receiver or trustee, or until the landlord takes possession through "reentry", he is entitled to all accrued and unpaid rent; thereafter (since he has possession of the premises or may take such possession) he is entitled to prove a claim only for the difference between the reasonable value of the use of the premises and the rent reserved in the lease, limited however to a sum amounting to not more than three years of rent.

The doctrine of the *Chicago Auditorium* case operated to give complete and equitable relief to parties to ordinary executory contracts. The extension of this doctrine operates to give similar relief to the parties to an executory lease of real estate. The tenant is relieved of future obligations under the lease. The landlord is given a provable claim against the estate of his tenant.

By interpreting the rent claim provisions of Section 77B as extending the doctrine of the *Chicago Auditorium* case to leases, an equitable and logical solution of all problems dealing with claims under leases may be had. Any other interpretation of the language of Section 77B results in inconsistencies and confusion. This is illustrated by the difficulties experienced by the Court below in passing upon a landlord's claim under a lease containing a covenant of indemnity (See discussion of *Kuhner* case, *infra*, pp. 22-4).

POINT IV

The decision of the Court below on the Kuhner claim [*Kuhner* v. *Irving Trust Co.*, 85 F. (2d) 35] is contradictory to its decision on the claim in this case.

In the *Kuhner* case, as in this case, the trustee in the prior bankruptcy proceeding rejected the lease. In each case the landlord reentered after such rejection. In the *Kuhner* case the lease contained a covenant of indemnity under which it was agreed that if the lessee should be adjudicated a bankrupt the landlord might reenter and the lessee would then "indemnify the Landlords against all loss of rent which the Landlords may incur by reason of such termination during the residue of the term" [85 F. (2d) 35, at 36]. In the case at bar the lease contained no such covenant. The Circuit Court of Appeals allowed the claim in the *Kuhner* case but denied the claim in the case at bar.

In the *Kuhner* case, the Court correctly held that an absolute liability of the lessee on the covenant of indemnity was created by the bankruptcy of the lessee and the reentry of the landlord, and that such liability still existed when the proceedings under Section 77B were initiated. However, instead of allowing a claim on the liability created by this covenant, the Court allowed the claim as for an injury resulting from the rejection of the lease in bankruptcy.

In the *Kuhner* case the landlord had no "claim against a lessee for damages or indemnity under a covenant contained in a lease which would have been recoverable in a civil action had there been no 77B petition approved * * *" (which was the test applied by the Court in *In re United Cigar Stores Co. of America* (*Otis*), 83 F. (2d) 202, 206, and in this case).

The amount of the claim on the Kuhner covenant of indemnity was too speculative to be proved or recovered under applicable state law until the end of the original term of the lease (*Hermitage Co.* v. *Levine,* 248 N. Y. 333).

In addition, the claim actually allowed was different from, and contradictory to, the claim given to the landlord by the express language of the covenant. Under the covenant of indemnity, the claim was to be measured by the difference, at the end of the term of the lease, between the amounts of rent actually collected by the landlord during the term and the total rents to be paid under the lease. The Court permitted the claim "to be liquidated like a claim for breach of an executory contract for chattels; that is, by discounting the future payments and subtracting the appraised value of the term from their sum". [85 F. (2d) 35, at 37.]

In spite of its statement that "we cannot suppose that Congress was trying to make over the contract" [85 F. (2d) 35, at 37], the Court actually *did* make over the contract of indemnity by allowing a claim which was not based on such contract of indemnity. As this Court stated in *Manhattan Properties* v. *Irving Trust Co.,* 291 U. S. 320, at 337:

> "* * * These [indemnity covenants] do not provide for liquidation of damages (compare *Wm. Filene's Sons Co.* v. *Weed, supra*), nor indeed for any right to damages for breach of the covenant to pay rent."

The result reached by the Court in determining the Kuhner claim was sound. The claim was properly liquidated "like a claim for breach of an executory contract for chattels" [85 F. (2d) 35, at 37.] But this conclusion is warranted only on the theory that Section 77B gives the same provable claim on an executory lease as on any other executory contract; that the damages resulting from the breach of the covenant of indemnity in the

Kuhner lease were too speculative to admit of reasonable proof; and that the claim was therefore measured as though the lease contained no covenant for damages or indemnity.

On this theory, petitioner in the case at bar was entitled to the allowance of its claim.

POINT V

Surrender or reentry after the rejection of a lease does not deprive the landlord of his right to prove a claim. On the contrary, it is a condition precedent to proof of the injury resulting from the rejection.

Section 77B(b) (10) provides that the claim of a landlord resulting from the rejection of an unexpired lease shall be: (1) for all "unpaid rent accrued up to such *date of surrender or reentry*"; plus (2) "an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the *date of surrender* of the premises to the landlord or the *date of reentry* of the landlord, whichever first occurs, * * *." (Italics ours.)

No claim is provable until after there has been either a "surrender of the premises to the landlord" or a "reentry of the landlord".

Surrender or reentry by the landlord does *not* take away the remedy given by Section 77B. It is a condition precedent to the provability of the claim. Without a surrender or reentry there is no prescribed method for fixing the amount of the claim.

Even aside from the express provision in Section 77B, it is obvious that the landlord's claim may be measured only if the lease is terminated. An obligation to pay rent remains against the tenant so long as the lease is alive. While this liability exists, the amount of the landlord's

damage will be contingent upon the rent paid in the future by the tenant or his assignee. If this possibility of performance is not eliminated, the damage to the landlord will be too speculative to be proved. One of the grounds for not allowing rent claims in bankruptcy prior to the amendment of Section 63(a) of the Bankrupcty Act in 1934, was "because of the uncertainty at the date of adjudication that the lessor will reenter" (*Manhattan Properties* v. *Irving Trust Co.*, 291 U. S. 320, 331).

The original rent provision in the Bill which enacted Section 77B (H. R. 5884, 73rd Cong., 1st Sess., 77 Cong. Rec. 5009-5013, June 5, 1933) declared that a claim under a rejected executory contract would be allowed "provided such contract shall not have terminated by forfeiture, reentry, or otherwise." The omission of this language in the Act as passed must be taken as a clear indication of a change in the intent of Congress.

POINT VI

Section 77B grants the right to prove a claim where a lease was rejected and terminated prior to the enactment of Section 77B in a bankruptcy proceeding which was still pending when the proceedings under Section 77B were initiated.

Section 77B (b) (10) gives the landlord the right to prove a claim for the resultant injury "In case an * * * unexpired lease of real estate * * * shall have been rejected by a trustee or receiver in *bankruptcy* * * * *in a proceeding pending prior to the institution of a proceeding under this section* * * *." It also provides that the limitation of the landlord's claim shall be measured from "the date of surrender of the premises to the landlord or the date of reentry of the landlord, * * * *whether before or after the filing of the petition* * * *" (Italics ours.).

This language is clear. No argument seems necessary to establish the intent of Congress to bestow upon the landlord a claim for injury caused by the rejection of his lease in a prior bankruptcy proceeding, even if the premises were surrendered to the landlord, or he reentered, "*before* * * * the filing of the petition * * *" initiating the proceedings under Section 77B. (Italics ours.)

The provisions of Section 77B are applicable to debtors and creditors whose interests were acquired *prior* to the enactment of Section 77B and to proceedings in bankruptcy which were pending at the time of such enactment.

> "(p) This section shall take effect and be in force from and after the date of the approval of this amendatory Act, and *shall apply as fully to debtors,* their stockholders *and creditors, whose interests or debts have been acquired or incurred prior to such date,* as to debtors, their stockholders and creditors, whose interests or debts are acquired or incurred after such date. *Proceedings under this section may be taken in proceedings in bankruptcy which are pending on the effective date of this amendatory Act*" (Italics ours.).

Almost identical language was used in the enactment of Sections 74, 75 and 77 of the Bankruptcy Act in March, 1933:

> "* * * This Act shall take effect and be in force from and after the date of its approval, and shall apply as fully to debtors, their stockholders and creditors, whose interest or debts, whether secured or unsecured, have been acquired or incurred prior to such date, as to debtors, their stockholders and creditors, whose interest or debts have been acquired or incurred after such date. Proceedings under section 1 of this Act may be taken in proceedings in bankruptcy which are pending on the effective date of this Act."
>
> Sec. 2 of Public Law No. 420, 72d Cong., 2d Sess. (Mar. 3, 1933), Chap. 204, 47 Stat. 1467, at 1482.

Commenting on this language, the Circuit Court of Appeals for the Seventh Circuit said:

> "Considering the remedial character of the legislation and the comprehensiveness of the above-quoted words, we are left in little doubt as to its construction.
>
> "Certainly, Congress intended by this amendment to provide for the more effective and satisfactory administration of the estate of an insolvent debtor or of a debtor who, having property, was nevertheless unable to meet his obligations as they matured, than was possible under the act before it was amended. In view of the purpose, it was both natural and logical for Congress to make available the remedies which the new act provided, to those who had begun, and against whom there had been begun, bankruptcy proceedings before March 3, 1933, but whose estates were still being administered in the courts of bankruptcy. To limit the language to instances where involuntary petitions had been filed in bankruptcy but wherein no adjudication had occurred would not only largely nullify its effect but would be contrary to the wording of the above-quoted provision and violative of the purpose of the legislation."
>
> *Grzenia* v. *Lucius*, 66 F. (2d) 349, 350.

In the absence of language indicating a contrary intent, a statute containing a new procedure or providing a new remedy is deemed to apply to conditions existing at the time of its enactment.

> "Statutes regulating legal remedies are generally construed as operative upon an existing condition of things as well as upon conditions to arise after their enactment. 'Where a new statute deals with procedure only, *prima facie* it applies to all actions—those which have accrued or are pending and future actions.' (Sutherland on Statutory Construction, p. 630.)"
>
> *Laird* v. *Carton*, 196 N. Y. 169, 171.

A consideration of the conditions which existed at the time when Section 77B was enacted makes it manifest that

Congress intended to give relief to landlords who had been unjustly deprived of their rights by the rejection of leases in bankruptcy proceedings prior to the enactment of Section 77B.

The Debtor and other chain store corporations with numerous executory leases had voluntarily instituted bankruptcy proceedings in 1932. Although bankruptcy proceedings are usually intended for liquidation rather than reorganization, and these corporations desired reorganization, they went into bankruptcy because it afforded them an opportunity to avoid more lease claims than in an equity receivership.

The use of bankruptcy proceedings merely to cut off the claims of landlords was generally criticized, and almost became a national scandal. The facts were well known to the members of Congress. It was natural therefore for Congress to provide in Section 77B that a corporation desiring to discontinue pending bankruptcy proceedings and avail itself of the benefits of reorganization under Section 77B, could do so only if it granted the landlord a provable claim for the injury which he had previously sustained by the rejection of his lease in bankruptcy.

That the provision in Section 77B relating to a rejection of an unexpired lease in a prior proceeding was included with specific reference to rejections which had occurred prior to the enactment of Section 77B becomes further apparent when it is realized that in the future the spectacle of a corporation first being subjected to bankruptcy proceedings and then having its administration transferred to proceedings under Section 77B is bound to be rare. The more likely procedure will be to attempt rehabilitation of the corporation under Section 77B first and to resort to liquidation only when the futility of reorganization becomes evident. It seems therefore that corporations which were in bankruptcy when Section 77B was enacted were the particular debtors against whom these rent provisions were directed.

The amendment of Section 63(a) of the Bankruptcy Act, in June, 1934, also serves to reveal the intent of Congress to afford new remedies to persons interested in proceedings instituted before the amendments were enacted. The first amendment [48 Stat. 923, 924], adopted on the same day as Section 77B, made the new rent provisions of Section 63(a) applicable to "estates pending at the time of the enactment of this amendatory Act". Shortly thereafter, a further amendment [48 Stat. 991] made the rent provisions of the amended Section 63(a) applicable only to pending estates in which the time for filing claims had not expired. The original amendment was obviously intended to apply to claimants in *all* proceedings pending at the time of its adoption, for otherwise the subsequent amendment would have been unnecessary.

The limitation imposed by the second amendment of Section 63(a) was desirable in bankruptcy proceedings because of the confusion which would result if pending estates were required to reopen their proceedings after the time to file claims had expired. A similar limitation was not inserted in Section 77B. It was not required. No proceedings under Section 77B were, of course, then pending.

POINT VII

The grant of the right to prove a claim for the injury caused by the rejection of a lease in a bankruptcy proceeding pending when Section 77B was enacted is not unconstitutional.

This Court has already stated that Congress may grant a provable claim for future rents under a lease which has no covenant for damages or indemnity.

> "The issue is not one of power, for plainly Congress may permit such claims or exclude them. * * *"
>
> *Manhattan Properties* v. *Irving Trust Co.*, 291 U. S. 320, 332.

No constitutional rights of a debtor, or of any of its creditors or stockholders, are invaded by granting a landlord a right to prove a claim for the damages sustained by him as a result of a rejection of his lease *before* the enactment of Section 77B in bankruptcy proceedings which were pending when Section 77B was enacted and which are subsequently merged into the 77B proceedings.

Creditors who extended credit after the filing of the petition in bankruptcy enjoy the priority which attaches to all expenses of administration and will therefore be paid in full before any distribution is made to the landlord. Such creditors can not be injured by the allowance of the landlord's claim.

The creditors with whom the landlord is permitted to participate on a parity in the distribution of the debtor's assets under Section 77B extended credit before the filing of the petition in bankruptcy and therefore at a time when the landlord's lease was a valid and subsisting obligation of the debtor. Such creditors can not claim that assurances upon which they relied in extending credit have been defeated. As the Court said in *In re Inland Dredging Corp.*, 61 F. (2d) 765, 766, "All that was done was to provide for a new division of any pot, which should in the future arise through the sequestration of the debtor's assets in bankruptcy, or any other insolvency proceedings".

With knowledge of the plight of this Debtor and of some of the other large chain store corporations which had utilized bankruptcy proceedings to cut off rent claims without intending to liquidate their enterprises in the manner prescribed by the Bankruptcy Act, Congress deliberately extended relief to such corporations by affording them a new vehicle for reorganization. But as a condition to use of the new procedure by corporations *already in bankruptcy*, Congress provided that landlords injured by the rejection of leases in the bankruptcy proceedings must be permitted to prove claims for the injury which resulted from such rejections.

Although this Debtor *voluntarily* initiated the proceedings under Section 77B, it now proposes to accept the benefits of the new procedure without submitting to its burdens. It desires to utilize the new procedure without complying with the conditions which Congress imposed upon the acceptance of the benefits.

The Debtor had no constitutional right to the use of Section 77B. Congress could have provided that the new procedure be available only to corporations not already in bankruptcy. When it conditioned the use of this procedure upon a recognition of landlords' claims for injuries inflicted in the bankruptcy proceedings, Congress was therefore well within its constitutional power.

Having voluntarily accepted the benefits of Section 77B, the Debtor is estopped from denying the validity of the conditions precedent to its acceptance of such benefits. Since it is already in proceedings under Section 77B, it is particularly estopped from denying the validity of conditions without the performance of which it is not entitled to be in such proceedings.

Section 77B regulates the distribution of the assets of a debtor in the possession of the bankruptcy court. It does not redefine or change the substantive law of landlord and tenant.

The proceeding initiated by this Debtor under Section 77B is merely a continuance of the prior bankruptcy proceeding in which the petition initiating the 77B proceeding was filed and in which this landlord's lease was rejected. The proceeding under Section 77B is "an amplification or new end product of the original bankruptcy, just as though the bankrupt or the alleged bankrupt had proposed a composition, * * *" (*In re Paramount Publix Corp.*, 85 F. (2d) 42, 44).

> "* * * The bankruptcy proceeding is indeed truncated midway and not allowed to conclude as it began; but the graft does not make it a new growth from the root, and the result is certainly meant to be an organic whole."
>
> *In re Paramount Publix Corp.*, 85 F. (2d) 42, 45.

Before the petition in bankruptcy was filed, the landlord had the same right as other creditors to look to the assets then owned by the Debtor for the satisfaction of his claim. It was the bankruptcy proceedings, combined with the bankruptcy trustee's failure to assume or adopt the lease, which took away the landlord's right to look to the bankrupt's assets as of the filing of the petition for the satisfaction of his claim.

All that the landlord requests, and all that Section 77B gives, is the right, as a creditor of the Debtor at the time the petition in bankruptcy was filed, to participate equitably with other creditors, having claims at that time, in the distribution of the assets which belonged to the Debtor on that date. To give effect to the intent of Congress and permit the landlord to participate in the distribution of the assets does not involve the recognition of a new claim not previously existing; it involves merely the recognition of a new remedy for the deprivation of the landlord's rights as they existed when the petition in bankruptcy was filed. By failing to adopt the lease, the trustee effectively divested the landlord of his remedy against the Debtor's assets. Congress has now given a new remedy for the injury resulting from the rejection of the lease and for the breaches which occurred both before and after the rejection.

Congress may, in the exercise of its power over the subject of bankruptcies, give a provable claim for an injury not previously recognized even though the incidental effect may be a reduction in the payments which would otherwise be made to other creditors.

Having power to regulate the currency, Congress may make paper money legal tender, even though a loss results to a creditor who must now accept a depreciated medium in satisfaction of his claim. *Legal Tender Case,* 110 U. S. 421. Under the same power, Congress may commandeer

metal or may cut down the rights of individual ownership in metal. *Ling Su Fan* v. *United States,* 218 U. S. 302. A valid claim to gold created by express provision of contract may be destroyed. *Norman* v. *B. & O. R. Co.,* 294 U. S. 240, 307, 308. By its power over interstate carriers, Congress may prohibit free transportation even though its mandate results in depriving an individual of a vested right to such transportation. *Louisville & Nashville R. R. Co.* v. *Mottley,* 219 U. S. 467, 482. In the interests of interstate commerce, Congress may direct an increase in intrastate rates which will nullify a right to lower rates acquired by the people of a state through express contract. *New York* v. *United States,* 257 U. S. 591.

So it is with the bankruptcy power. It was created so that Congress might have jurisdiction over the affairs of an impecunious debtor in the interests of an orderly and equitable readjustment. The power existing, its use can not be made to depend upon reasonable incidental effects.

When a creditor first acquires his claim, he obtains no right in the bankruptcy remedy then existing which is absolute and certain to remain fixed. His right is subject to the power over bankruptcies and it must yield to an exercise of this power. Congress may enact new and different relief for insolvent debtors and their creditors.

> "There was no vested right in the bankrupt to have the law stand as it was. No one would seriously question the right of Congress to modify the law, and state the conditions upon which debtors in the future could be discharged from their indebtedness, and, when the bankrupt made his application for a discharge in this proceeding, he invoked the law as it then was; and, under the statute of 1903, as we view it, the fact that he had been previously discharged from his indebtedness in a voluntary proceeding within six years was a statutory ground for withholding a second discharge upon his own application in this subsequent involuntary proceeding."
>
> *In re Seaholm,* 136 Fed. 144, 147.

The cases declaring that a *state* may not grant additional exemptions to debtors after creditors have extended credit and thereby deprive the creditors of their right, in state court proceedings, to look to such assets for the satisfaction of their claims, are not applicable. None of the cases decided on this point by this Court involved the exercise by Congress of its constitutional power over the "subject of bankruptcies". See *Edwards* v. *Kearzey*, 96 U. S. 595; *Bank of Minden* v. *Clement*, 256 U. S. 126.

Nor is the power of Congress in the exercise of its jurisdiction over the subject of bankruptcies involved in the cases dealing with the power of a state legislature over vested contract and property rights. See *Pritchard* v. *Norton*, 106 U. S. 124, 132; *Ballantine* v. *Macken* (N. J. Ct. of Err. & App.), 110 Atl. 910; *People* v. *Prather*, 343 Ill. 443, 175 N. E. 658; *State* v. *Shelton*, 138 Tenn. 345, 197 S. W. 1096; also 12 C. J. 973.

In Section 64 of the Bankruptcy Act [30 Stat. 563 (1898), as am'd, 32 Stat. 800 (1903), as am'd, 34 Stat. 267 (1906), as am'd, 44 Stat. 666 (1926), 11 U. S. C. A. § 104], Congress has provided certain priorities in the distribution of bankrupt estates. As a result, creditors who otherwise would share equally are relegated to a subordinate position. They are thus deprived of substantial rights originally possessed by them. But since the deprivation is incidental to an exercise of the power over bankrupt estates, there has been no violation of the Fifth Amendment. See *United States* v. *Fisher*, 6 U. S. (2 Cranch) 358.

Priorities given under an existing bankruptcy statute may be changed by a subsequent statute, and such a change is effective even as to claims arising prior to the change. *In re Inland Dredging Corp.*, 61 F. (2d) 765; *City of Chelsea* v. *Dolan*, 24 F. (2d) 522.

> "We cannot doubt the power. The act is remedial—to be liberally construed. Chelsea, on this record, had

no lien upon or vested right in the estate for its taxes; it had nothing but a claim under the Bankruptcy Act. It grounds its contention on this act, not on a lien under the statutes of Massachusetts. Congress has plenary power to pass uniform bankruptcy acts. 7 C. J. 18, and cases cited. It may amend or repeal at pleasure, provided it does not disregard the requirement of uniformity."

City of Chelsea v. *Dolan*, 24 F. (2d) 522, 523.

In the *City of Chelsea* case, *supra*, the court held the change applicable even though it became effective after the filing of the bankruptcy petition. In the *Inland Dredging Corp.* case, *supra*, the statute became effective before the filing of the petition in bankruptcy although after the debt was incurred.

Under its power over the subject of bankruptcies, therefore, Congress may change the order of priority in the payment of claims in bankruptcy proceedings, even after the claims have come into existence, thereby, in many instances, insuring payment in full to some classes of creditors while other classes receive nothing, in spite of the fact that the claims of both classes had equal priority under the state law and under the bankruptcy law at the time the claims arose.

It seems equally clear that Congress may permit a landlord, who had a valid and subsisting contract with the Debtor when the court took custody of its assets, to participate with other creditors in the division of such assets for the injury sustained by him through the deprivation of his right to look to the Debtor's assets for the satisfaction of his claims under the lease.

If the rights and remedies of all of the parties are actually fixed and crystallized by the bankruptcy proceeding, and such rights and remedies are only those which existed immediately prior to the filing of the petition under

Section 77B, then the use of proceedings under Section 77B by this Debtor is improper and illegal, and any creditor may insist on his right to have the assets of the Debtor liquidated as in bankruptcy in order that he may obtain the cash dividend which he would receive if the bankruptcy proceedings were consummated.

POINT VIII

The interpretation of the Court below makes redundant and of no effect the provisions in Section 77B granting the landlord a claim for the rejection of his lease.

The theory of the Circuit Court of Appeals, that no claim is provable unless the lessor has a claim under applicable state law or under a covenant for damages or indemnity when the 77B proceedings are initiated, ignores the fundamental basis of the remedy given to the landlord by Section 77B. It erroneously fails to base the claim upon a *rejection* of the lease, or even upon the lease itself. It bases the claim upon a debt created under state law by a prior breach of the lease, or upon a new contract for damages or indemnity arising under a covenant in the lease upon its termination (*Manhattan Properties* v. *Irving Trust Co.*, 291 U. S. 320, 338).

All debts and contract claims which are valid and enforcible against the debtor when the petition under Section 77B is filed are provable in the proceedings. No additional language is required to make provable a claim upon a debt or contract for damages or indemnity merely because it arises out of the breach of a lease. If the interpretation of the Court below is correct, therefore, the express language granting a landlord a claim for the rejection of his lease is redundant and without effect.

The Court below said that the language in Section 77B which gives the landlord a claim for the injury sustained by the rejection of his lease was intended "to make some valid claims [recognized under applicable state law] *provable* in proceedings under Section 77B which were not before provable in bankruptcy". (Italics ours.) [Opinion below in this case, 83 F. (2d) 209, 211]. This portion of Section 77B is not needed to make such claims provable. Section 77B elsewhere makes existing claims "provable" regardless of whether they would have been provable in ordinary bankruptcy proceedings. Subdivision (b)(10) provides that the term "creditors" shall include "holders of claims of whatever character against the debtor or its property, including claims under executory contracts whether or not such claims would otherwise constitute provable claims under this Act". (Italics ours.)

It has been argued that a claim under a lease rejected in a prior proceeding is provable only if the lease survives until the initiation of the proceedings under Section 77B. If this were the case, the bankrupt's continuing obligation under the lease could only be terminated by a rejection of the lease in the proceedings under Section 77B. The landlord's claim in that event would arise under the provision of Section 77B which gives a claim for the injury resulting from a rejection in the proceedings under Section 77B. Section 77B(b)(10), however, grants landlords the right to prove a claim for the resulting injury not only when a lease "shall be rejected * * * in a proceeding instituted under this section", but also when a lease "shall have been rejected by a trustee * * * *in bankruptcy* * * * *in a proceeding pending prior to the institution of a proceeding under this section.*" (Italics ours.) The latter provision has no meaning and effect unless it is applied to a case in which the lease has been terminated after rejection in the bankruptcy proceeding and prior to the initiation of the proceedings under Section 77B.

If the interpretation of the lower Court is accepted, some interesting questions suggest themselves:

May the landlord under a lease containing no covenant for damages or indemnity preserve his rights, after a rejection of the lease, by refusing to reenter or accept surrender of the premises? If so, what happens to the premises which have been abandoned by the trustee in bankruptcy and which the landlord, in order to preserve his claim, refuses to reenter? May the landlord keep the lease alive as an obligation of the debtor, and thereby prevent an effective reorganization?

Is a landlord deprived of all future rights under the rejected lease as well as all rights to damages in the proceedings, even if he refuses to reenter and repossess himself of the premises?

May Congress, under the Constitution, deprive the landlord of all rights under his lease, without compensation, if the benefits of such deprivation are given to the tenant (through its stockholders)?

It is respectfully submitted that the purposes of the reorganization proceedings may be accomplished and justice done to both landlord and tenant only if Section 77B is interpreted as granting (in the absence of an express covenant) the same provable claim to a landlord whose lease has been rejected as is given to a party whose executory contract has been rejected.

JOHN GERDES,
JOHN GODFREY SAXE,
Amici Curiae.

November 17, 1936.

SUPREME COURT OF THE UNITED STATES.

No. 260.—October Term, 1936.

City Bank Farmers Trust Company, Assignee, Petitioner, *vs.* Irving Trust Company, Trustee of the Estate of the United Cigar Stores Company of America, et al. } On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[January 4, 1937.]

Mr. Justice Roberts delivered the opinion of the Court.

Certiorari was granted in this and three following cases involving the construction and validity of provisions of Section 77B of the Bankruptcy Act[1] which enlarge the category of provable claims to include one by a landlord for injury due to rejection of a lease, or for damages or indemnity under a lessee's covenant.

Florence H. Bugbee, the petitioner's assignor, leased to United Cigar Stores Company of America premises in Trenton, New Jersey, for a term commencing April 1, 1926, and ending March 31, 1946. August 29, 1932, the lessee was adjudicated a bankrupt upon its own petition. November 11, 1932, the respondent, as trustee in bankruptcy, rejected the lease and abandoned the premises, a portion of which had been sublet by the bankrupt. Without notice to the Cigar Stores Company the landlord relet portions of the building to subtenants in possession and let other portions to new tenants.

June 9, 1934, two days after the passage and effective date of Section 77 B, the Cigar Stores Company, as permitted by subsection (*p*), filed in the pending bankruptcy proceeding its petition for reorganization. In the latter cause the petitioner presented a proof of claim for injury resulting from the rejection of the lease. The trustee objected to the claim and asked to have it expunged for the reason that the lease incorporated no covenant to indemnify the lessor for loss of rents or other provision enabling her to hold the tenant for damages or for rent accruing subsequent to termina-

[1] Added to the Bankruptcy Act of 1898 by Act of June 7, 1934, c. 424, § 1, 48 Stat. 912, as amended by Act of Aug. 20, 1935, c. 577, 49 Stat. 664, and Act of Aug. 29, 1935, c. 809, 49 Stat. 965; 11 U. S. C. 207.

tion of the leasehold estate, and asserted the leasehold had been terminated and all obligations of the debtor under the lease extinguished by the landlord's reentry and releting.

The special master who heard the cause recommended disallowance of the claim in the view that Section 77 B did not, and could not, create any valid and legal claims against the debtor where none existed anterior to the enactment of the section, and held that none existed before its adoption because, by the law of New Jersey, the landlord's reentry and releting worked a surrender of the leasehold. In his report the master referred to the fact that the record in the earlier bankruptcy proceeding disclosed a claim filed by the landlord, upon which dividends had been paid, for expenditures in restoring a party wall and closing up a common entrance in the leased building based upon the debtor's agreement to restore it at the expiration of the term, which was again asserted in the present proceeding. He thus commented upon this situation:

"Naturally, the entire basis of this claim for restoration is the expiration of the lease. The Trustee may well point to it, as showing that the Landlord, prior to the enactment of Section 77-B, by her re-entry and releting of the premises as aforesaid, considered that the lease terminated and expired."

The District Court approved the master's report and rejected the claim; and the Circuit Court of Appeals affirmed,[2] holding that the injury specified in Section 77B (b) (10) for which a claim by a landlord is allowable can only be such injury as would found an action under applicable state law. The court concluded that although according to the law of New Jersey the reentry and releting did not effect a surrender, the restoration of the building was such an assertion of dominion by the landlord as to deprive her of any further claim against the tenant.

The parties differ with respect to the correctness of the Circuit Court of Appeals' interpretation of the law of New Jersey. They also disagree as to whether the record supports the finding that the landlord restored a portion of the leased building. The disputes need not be resolved if the petitioner is right in asserting that, within the purview of Section 77 B, the lessor was a person injured by the rejection of the lease who is accorded a provable claim against the debtor's estate for the injury, notwithstanding the reentry, releting, and restoration of the premises, after rejection of the lease,

[2] 83 F. (2d) 209.

consummated a surrender of the leasehold, and ended the tenant's liability under the local law. As Section 77 B supplements and extends the bankruptcy system in force at the time of its enactment, we shall examine the question in the light of the old law, the supposed mischief arising under it and the alterations made by the later act.

1. Section 63 (a) of the Bankruptcy Act of 1898 [3] stated what claims should be provable in bankruptcy. The section gave a landlord no provable claim for rent to accrue after the trustee's rejection of a lease. The tenant's liability for future rent was not discharged and remained enforceable as instalments of rent fell due. This was necessarily so, since future rent is demandable only in the amounts and at the times named in the lease and the total cannot be recovered at law in a lump sum in advance of accrual of the instalments. This state of the law involved elements of hardship to both lessor and lessee. In the case of a corporate, and often in that of an individual lessee, the landlord's right to collect rent from a bankrupt tenant was valueless. On the other hand, if the landlord, notwithstanding rejection by the trustee, was compelled by its terms, or elected pursuant to its provisions, to treat the lease as still in force, he might throughout the remainder of the term harass the discharged bankrupt by successive actions for accruing rent and so retard or prevent the debtor's financial rehabilitation which the statute was intended to aid.

Many leases provide for the termination of the tenant's estate upon his adjudication as a bankrupt, by the lessor's reentry. Under the old law such termination did not give rise to a provable claim for future rent, or for damages, or for indemnity. Not uncommonly lease agreements, in addition to stipulation for termination of the leasehold upon the tenant's bankruptcy, provide that the bankrupt shall indemnify the landlord for loss of future rent. These provisions vary in their terms, some requiring the rendition of indemnity as each instalment of rent falls due, others at the end of the term when the full difference between the rent reserved and that received upon reletting can be ascertained. Under Section 63 (a) of the Act of 1898 such covenants did not support a provable claim, as the obligation to indemnify ripened after adjudication. The consequence was that liability under this sort of covenant was not discharged and remained to haunt the bankrupt.

[3] 30 Stat. 562.

As early as 1932 proposals were brought forward in Congress for the broadening of the bankruptcy system to authorize proceedings for the reorganization of business corporations. Bills authorizing proceedings in courts of bankruptcy to that end failed of passage in the 72d and 73d Congress. H. R. 5884, 73d Congress, Second Session, which ultimately became law as Section 77 B of the Bankruptcy Act was under consideration when the decision in *Manhattan Properties, Inc.* v. *Irving Trust Company,* 291 U. S. 320, threw into high relief the plight in which landlords found themselves as a result of the flood of corporate bankruptcies brought about by the economic depression. The situation of owners of business properties leased to chain store organizations which had resorted to voluntary bankruptcy largely as a lever to force revision of leases was the subject of comment in and out of Congress. By the same act Section 63 (a) was amended to give a provable claim to a landlord whose lease had been rejected by a trustee in bankruptcy and a similar provision was incorporated in 77 B, the new reorganization section. This history cannot be ignored in construing the supplemental legislation.

2. The purpose of Section 77B was to facilitate rehabilitation of embarrassed corporations by a scaling or rearrangement of their obligations and shareholders' interests, thus avoiding a winding up, a sale of assets, and a distribution of the proceeds. A salient element in such a reorganization is the discharge of all demands of whatsoever sort, executory and contingent, presently due or to mature in the future. Of such claims not the least important are those for rent to accrue under a lease, or for damages or indemnity payable because of the termination of a leasehold. Obviously if such obligations are to be discharged they must be made provable, for they cannot be destroyed. How, then, did the Congress deal with them?

The pertinent provisions of Section 77B are copied in the margin.[4]

Clause 10 renders provable claims upon covenants of indemnity maturing upon reentry after adjudication. The term "creditors"

[4] "(*a*) Any corporation which could become a bankrupt under section 4 of this Act, . . . may file an original petition, . . . in any proceeding pending in bankruptcy, whether filed before or after this section becomes effective. . . ."

"(*b*). . . . (10). . . . The term 'creditors' shall include for all purposes of this section and of the reorganization plan, its acceptance and confirmation, all holders of claims of whatever character against the debtor or its

is made to include "holders of *claims* of whatever character against the debtor or its property, including claims under executory contracts, *whether or not such claims would otherwise constitute provable claims under this Act.*" Bankruptcy of the obligor is an anticipatory breach of an executory contract and a claim for damages for the breach was provable under § 63 (a) of the Act of 1898.[5] One having a demand against a debtor whose affairs are in the hands of an equity receiver, if the claim matured after the receiver's appointment but before the expiration of the period fixed for presentation of claims, is entitled to prove and to share in distribution;[6] but the rule in bankruptcy has been that the claim under an executory contract must mature at or before the filing of the petition.[7] The language which is italicized in the foregoing quotation from clause 10 can have no other meaning than that claims upon covenants for damages or indemnity arising out of the termination of a lease after initiation of proceedings under Section 77B are provable. The provision, however, creates no new claim. It merely treats the adjudication as a breach of covenant and gives a provable claim in virtue of the breach.

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property, including claims under executory contracts, whether or not such claims would otherwise constitute provable claims under this Act. The term 'claims' includes debts, securities, other than stock, liens, or other interests of whatever character. . . .

"In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity, in a proceeding pending prior to the institution of a proceeding under this section any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor. The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63 (a) of this Act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or reentry: . . ."

"(*p*) This section shall take effect and be in force from and after the date of the approval of this amendatory Act and shall apply as fully to debtors, their stockholders and creditors, whose interests or debts have been acquired or incurred prior to such date, as to debtors, their stockholders and creditors, whose interests or debts are acquired or incurred after such date. Proceedings under this section may be taken in proceedings in bankruptcy which are pending on the effective date of this amendatory Act."

[5] *Chicago Auditorium Association* v. *Central Trust Company*, 240 U. S. 581.

[6] *Wm. Filene's Sons Co.* v. *Weed*, 245 U. S. 597, 601-602.

[7] *Manhattan Properties, Inc.* v. *Irving Trust Company, supra.*

Since in the instant case the lease contains no such covenant, in the absence of some further provision respecting landlords' claims the petitioner would be without remedy under Section 77B as it would have been in strict bankruptcy proceedings under Section 63 (a) of the Act of 1898 until that section was amended in 1934. There is, however, a further provision: "In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge [See subsection (c) (5).] given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity, in a proceeding pending prior to the institution of a proceeding under this section *any person injured* by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor." Under the old law the rejection of a lease by a trustee in bankruptcy was not a breach of the lease, in the absence of a specific agreement that it should be so. The bankrupt tenant remained liable for the rent as it fell due but all the assets wherewith he might pay were taken from him. For a default in payment subsequent to adjudication the landlord might reenter and terminate the lease. By virtue of a covenant so providing the landlord might treat the bankruptcy as cause for reentry and termination of the leasehold estate. While, therefore, the rejection of a lease by a trustee in bankruptcy might, and usually did, spell possible or probable injury to the landlord, that fact gave him no standing as a creditor in the bankruptcy proceeding. Having in mind this state of affairs the purpose is clearly to give a landlord a provable claim for injury due to the rejection of his lease, whether the instrument contains a covenant of indemnity or not.

Although, as we have noted, under the Act of 1898 rejection by the trustee was not a breach of the lease, it left the premises in the possession of an impecunious tenant with the virtual certainty they would be thrown back upon the landlord's hands untenanted. If the owner could not turn his property to account on terms as favorable as those embodied in the rejected lease obviously he suffered an injury.

The opinion in the *Manhattan Properties* case, *supra,* adverts to the fact that for many years the English bankruptcy acts have given a remedy for the loss of future rents due to supervening bankruptcy and sequent rejection of the lease.[8] Congress was familiar

[8] 291 U. S. at p. 332.

with this fact when Section 77B was under discussion.[9] The analogous provisions of the English Acts while differently phrased are of the same purport as those of Section 77B.[10] Congress intended to supply the omission of the Act of 1898 and to create a claim provable in a reorganization proceeding for injury due to a trustee's rejection. This conclusion finds further support in the succeeding sentence, which in limiting the amount allowable upon these claims, refers to them in three aspects, thus: "The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate *or* for damages *or* indemnity under a covenant contained in such lease", etc.

3. Like any other provable claim, that of a landlord for injury resulting from rejection of the lease, or for damages or indemnity for termination of the tenure, may, for an adequate consideration, be released, *Schwartz* v. *Irving Trust Company* (No. 436, post). The lease, moreover, may contain stipulations, fulfillment of which is to be full compensation for any loss due to termination of the leasehold and thus bar any claim under 77 B for the landlord's loss. *Meadows* v. *Irving Trust Company* (No. 151, post).

4. The question for decision in this case is whether the claim recognized by Section 77 B, which would not have been an enforceable demand at common law, or under the laws of many of the states, is allowable only if the leasehold estate has not, after rejection of the lease, been drowned by surrender effective under state law or otherwise terminated pursuant to state law by the lessor's conduct.

We think it clear that provability of such a claim is unaffected by any termination of the leasehold subsequent to rejection of the lease. The provision is that the landlord's claim for injury resulting from rejection, or for damages, or for indemnity under a covenant, shall be limited to an amount not exceeding the rent reserved "for the three years next succeeding *the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs*, whether before or after

[9] Cong. Rec., Vol. 76, Part 3, p. 2940.

[10] 32 & 33 Vict., c. 71, § 23 (1869); 46 & 47 Vict., c. 52, § 55 (1) (3) (7) (1883); 4 & 5 George V, c. 59, § 54 (1) (3) (7) (1914). The subject is first mentioned in the Act of 1869. The English acts authorize "disclaimers" of onerous property or contracts and specifically refer to leases. The provision for a provable claim based on a disclaimer is the same in the Acts of 1883 and 1914, "Any person injured by the operation of a disclaimer under this section shall be deemed to be a creditor of the bankrupt to the extent of the injury, and may accordingly prove the same as a debt under the bankruptcy."

the filing of the petition, ..." Plainly the word "reentry" is used to describe a case where the landlord, treating the bankruptcy as a breach of the lease, reenters for condition broken. Whether the other phrase, "surrender of the premises to the landlord", denotes the technical surrender which drowns the particular estate in the reversion, or the mere tradition to, and acceptance by, the landlord of possession, is immaterial. The amount of the landlord's claim for the loss of his lease necessarily is the difference between the rental value of the remainder of the term and the rent reserved, both discounted to present worth. This, we have said, is a method of liquidation familiar and fair. It was the method adopted under Section 77 B in *Kuehner* v. *Irving Trust Company, et al.*, 85 F. (2d) 35, the judgment in which is this day affirmed (No. 354, post). If the landlord must give credit for the present rental value of the premises he is entitled to avail himself of them for realization of that value, and this he cannot do without reentry and reletting. If he must give such credit he surely has the option to attempt recoupment of his loss by occupying the premises for the remainder of the term. But such occupation, under the law of most of the states, amounts to a complete termination of the leasehold and deprives the landlord of any further rights as lessor. It is evident that if a lease be rejected the subsequent repossession of the demised premises, and acts of control and dominion do not destroy the provability of a claim under Section 77B.

It is suggested that if a landlord desires to avail himself of the privilege accorded by the Section, he must keep the leasehold estate intact until his claim shall have been proved and allowed. In view, however, of the obvious intent of the statute to extend relief not only to landlords whose leases may in future be rejected, but also to those whose leases have been rejected in prior bankruptcy or equity proceedings, such a construction would ill accord with the remedial purposes of the act, which demand a liberal construction in favor of the claimants for whom relief was intended.

We conclude that the petitioner's claim should have been allowed. The judgment is reversed and the cause is remanded to the District Court for further proceedings in conformity with this opinion.

So ordered.

Mr. Justice BRANDEIS took no part in the consideration or decision of this case.